United States Court of Appeals

for the Second Circuit

APPELLANT'S BRIEF

ORIGINAL

75-1153

B P/S.

To be argued by
JAMES SCHREIBER

United States Court of Appeals
FOR THE SECOND CIRCUIT

DOCKET NO. 75-1153

UNITED STATES OF AMERICA,

Appellee,

v.

JACKSON D. LEONARD,

Defendant-Appellant.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF FOR JACKSON D. LEONARD

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BRIEF FOR THE APPELLANT JACKSON D. LEONARD

Preliminary Statement

Jackson D. Leonard appeals from a judgment of conviction entered in the United States District Court for the Southern District of New York on March 7, 1975, after a seven-day jury trial before the Honorable Richard Owen, United States District Judge.

The indictment, 74 Cr. 599, filed June 13, 1974, charged Leonard, in two counts, with making and subscribing, under penalties of perjury, income tax returns for 1967 and 1968 which omitted income from reported adjusted gross income, in violation of 26 U.S.C. § 7206(1).*

Trial began January 13, 1975 and the jury returned verdicts of guilty on both counts on January 21, 1975.

* Count One related to 1967 and Count Two to 1968. A third count charging Leonard with a violation of 18 U.S.C. § 1001 was dismissed before trial. Leonard was not charged with tax evasion, 26 U.S.C. § 7201.

The text of § 7206(1) is set forth in the Addendum to this brief at page 1.

Judge Owen sentenced Leonard to eighteen months imprisonment, but suspended execution of all but three months, and imposed the maximum fine of $10,000 ($5,000 on each count), plus the costs of prosecution. Execution of sentence has been stayed pending appeal.

Statement of the Issues

1. Should this Court follow the First and Fourth Circuits in requiring the IRS to comply with its own regulations governing the conduct of criminal tax fraud investigations and reverse the conviction for failure to advise Leonard of his constitutional rights?

2. Did the IRS mail watch (which intercepted *all* mail arriving from Switzerland at Kennedy Airport during two entire four month periods in 1968 and 1969) violate Post Office regulations, the First and Fourth Amendments, and Swiss law and should evidence obtained as a result of the mail watch have been suppressed?

3. Did the prejudicial and inflammatory effect of the government's "similar act" evidence relating to Swiss bank accounts outweigh its probative value so that such evidence should have been excluded, under *U.S.* v. *Deaton*, 381 F.2d 114 (2nd Cir. 1967)?

4. Does *Bronston* v. *U.S.*, 409 U.S. 352 (1973) bar proof of willfulness by means of an allegedly "false statement" which was not literally false?

5. Was the defendant denied a fair trial when the government obstructed his interviews with potential witnesses?

6. Was the defendant denied a fair trial under *U.S.* v. *Baum*, 482 F.2d 1325 (2nd Cir. 1973) where the trial court refused to grant a reasonable continuance for the defendant to meet surprise similar act proof?

7. Was the defendant denied a fair trial when the prosecutor in his opening charged that the defendant had committed other crimes and made other false statements which allegations were untrue and never proved?

8. Did the government fail to prove that the defendant had omitted income in 1967?

9. Did the court err when it refused to instruct the jury on the tax consequences of defendant's assignment to his corporation of his right to the income which he did not include in his 1968 return?

10. Did the court err when it failed to dismiss the indictment which was founded on materially false grand-jury testimony?

Statement of the Facts

Introduction

Jackson D. Leonard is 59 years old and the father of four children. (A 38)* He is a highly regarded scientist and chemical engineer who specializes in designing complex chemical plants throughout the world, including the United States, Canada, Belgium, Holland, Italy, Mexico, Australia, Rumania, India and Japan. (A 110-111, 39)

The income which Leonard allegedly failed to report was received from the Treadwell Corporation ("Treadwell") (A 24a, 36a, 37a, 497) in connection with a contract (the "UCC Contract") (GX 3) with Union Carbide Corporation ("UCC") which initially provided that Leonard would design two chemical plants for UCC, one in Taft, Louisiana and the other in South Charleston, West Virginia, but which later was amended to delete the South Charleston plant.

Until February 1, 1968, Leonard conducted business exclusively in the name of a sole proprietorship, The Leonard Process Co. ("Leonard Process"). Effective that date, with the consent of UCC, he transferred Leonard Process'

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* References to pages in the Appendix to this brief are preceded by "A". References to government exhibits at trial are designated "GX", defendant's exhibits as "DX" and court exhibits as "CX". "GXH" refers to government exhibits at the pretrial hearing on January 8, 1975 and "DXH" refers to defendant exhibits at the hearing.

assets, including the UCC contract, to Leonard Process Co., Inc. ("Leonard Corp."), a Subchapter S (tax-option) corporation wholly owned by him. (A 98-99) (GX 65) Consequently, payments from Treadwell through January, 1968 were made to Leonard Process and were reportable by Leonard in his personal tax return. After that date, they were payable to Leonard Corp. and reportable on the corporation's tax return, and Leonard, in turn, did not have to report income, if any, from the corporation until his 1969 tax return.

The Audit of Leonard's Tax Affairs

The underlying audit of Leonard's tax returns was precipitated by two independent events which occurred almost simultaneously. The first was that an undisclosed informant, who was seeking a reward, claimed that Leonard had been receiving commercial bribes, i.e., illegal kickbacks, from Treadwell.* The second was that a mail watch conducted by the Internal Revenue Service ("IRS") led the IRS to suspect that Leonard had a secret Swiss bank account. (A 334a)

The IRS Foreign Bank Account Project

In 1968, the IRS instituted a major, clandestine program to identify and prosecute American taxpayers who had dealings with Swiss banks (the "Foreign Bank Account Project" or "FBA Project").

The FBA Project was so highly secret that agents working on it were forbidden to discuss it even with other IRS personnel. (A 282-283a) A major aspect of the project was a mail watch conducted by Special Agents** of the IRS who

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* As the evidence at trial demonstrated, the Treadwell payments were, in fact, perfectly proper and in accord with the provisions of the UCC contract. (GX 3 ¶ 3(e))

** Special Agents work in the Intelligence Division of the Internal Revenue Service. They are the criminal investigators of the IRS; they have the right to carry guns and make arrests. *Revenue* Agents, (as opposed to *Special* Agents) are simply auditors, i.e.

(*footnote continued on following page*)

intercepted, inspected and photocopied mail coming into the U.S. from Switzerland. The mail watch was apparently commenced without consultation or coordination with the Department of Justice, which was engaged at the time in sensitive negotiations with Switzerland regarding a treaty under which Switzerland would disclose to American law enforcement agencies Swiss bank accounts owned by American citizens who were suspected of criminal activity. (A 387a-388a, 403a-404a)

In order to obtain authority for the mail watch, the IRS (under then current Post Office regulations) was required, as is explained more fully below, to represent in writing to the Post Office that the mail watch was part of a criminal investigation (*Postal Bulletin* 20478; *Part* 861 of the *Postal Manual*, See Addendum, p. 2 et seq.)

The mail watch involved an unprecedented effort by Special Agents of the IRS to intercept, handle and inspect *all* mail arriving at Kennedy Airport from Switzerland during the period of January through April of 1968 and 1969.* (A 397a-398a, 405a-407a) Utilizing machines that microfilmed 3600 pieces of mail per hour, the IRS photocopied every envelope which lacked a return address, since it is the practice of Swiss banks not to put their names or addresses on envelopes.** (A 375-381a)

(*footnote continued from preceding page*)

accountants, whose responsibility is to conduct *civil* audits in order to determine the correct income tax liability of a taxpayer. Revenue Agents, on occasion, work with Special Agents on fraud cases, i.e. criminal investigations, but then only under the direction of Special Agents. (A 365a-366a)

* The mail watch was designed to coincide with the mailing by Swiss banks of year-end and quarterly, as well as monthly statements. The idea was that "where you have situations where somebody has two or three items a month four months in a row, its a good indication that they are involved in some way". (A 380a)

** Since the microfilming took a few hours at least, and in some cases when the mail was heavy a second machine was brought in, (A 377a-378a) the number of envelopes which the Special Agents photographed may have exceeded 100,000. (A 398, 405a-407a)

As a result of the mail watch, the tax returns of untold numbers of addressees who the IRS suspected were receiving mail from Swiss banks were examined to determine which would be "good candidates" for audits. Selections were thereafter made of 110 of them, in the New York area alone, without regard to the normal criteria for determining which taxpayers should be audited. One of the taxpayers selected for this special audit was defendant Leonard. (A 364a-372a)

The audits of these 110 were supervised by Special Agent Hyman Boller and Revenue Agent Bernard Morris. The auditors were specially picked from a select fraud group in the Audit Division and given "several pages worth of specific things" they were expected to look for in these audits. (A 412a) These special items, which included telephone records, cable and telex charges and backs of checks, were designed to develop leads on Swiss accounts. (A 359a)

In FBA project cases, Revenue Agents conducted the audits, gave no constitutional warnings, and deliberately concealed that they were conducting criminal investigations. (A 414a) While the audits were in progress, Special Agents continued the mail watches, and envelopes from Switzerland to taxpayers under audit were intercepted, inspected and photocopied. (A 394a-397a)

If the examination of the taxpayers' records failed to disclose independent proof of Swiss bank accounts, the Revenue Agents were instructed how to obtain incriminating admissions from the taxpayer.

Despite the fact that the IRS had information that a taxpayer had contacts with a Swiss bank, during discussions with him, the Revenue Agent asked him whether he had any *foreign,* rather than *Swiss,* accounts. If he denied having any, the Revenue Agent was directed to dictate, for the taxpayer's signature, an affidavit so stating. The affidavit's purpose was apparently to commit the taxpayer in writing to false denials that could be utilized in subse-

quent prosecutions either as direct evidence of criminal activity (making criminal false statements to government agents in violation of 18 U.S.C. § 1001) or as circumstantial evidence of willfulness (to be used in a subsequent prosecution for tax violations). (A 370a)

The Audit and the Indictment

Defendant was notified that his returns had been selected for audit by a standard notice sent to his home (GXH 1). It contained nothing to alert him of the criminal nature of the examination.* (A 409a)

The audit was begun in June or July, 1968 by Revenue Agent Mortimer Laski of the FBA project. It was six years before the investigation was completed, and at least eight, and possibly as many as seventeen, IRS agents dealt directly with the taxpayer or his representative during the course of the investigation. (A 707a)

On June 13, 1974, two days before the statute of limitations ran for the 1967 tax year,** Leonard was indicted on two counts of subscribing tax returns which omitted $24,168.09 from reported adjusted gross income before deductions ("AGI") of $259,051.97 in 1967, and $58,684.42 from AGI of $134,276 in 1968. He was not charged with tax evasion.

Despite the tremendous effort undertaken by the IRS (and possibly as the result of the lack of continuity of examining agents), the IRS failed either to learn or understand that most of the income ($52,455.22 out of the total of $58,684.42) that the indictment charged Leonard with omitting to report on his personal tax return for 1968 belonged to Leonard Corp., rather than to Leonard himself, by reason of the assignment of the UCC contract to Leonard Corp. (A 355a)

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* The IRS had conducted civil audits of Leonard in almost every one of the preceding 20 years. (A 39a et seq.)

** Leonard filed his 1967 tax return on June 15, 1968, pursuant to an extension granted by the IRS.

Additionally, despite the fact that the indictment charged Leonard with subscribing false tax returns for 1967 and 1968, the government did not discover that the defendant had not signed or even seen his 1968 return until after the defendant had nearly completed presentation of his case. (A 707a-708a)

Pre-Trial Hearing

1. The mail watch and lack of constitutional warnings.

Prior to trial, the defendant moved in the alternative to dismiss the indictment or to suppress evidence on the grounds that: (a) the evidence was improperly obtained through an unlawful mail watch; and (b) Leonard's incriminating statements were made without his being informed of his constitutional rights. Although the government conceded that no constitutional warnings had been given (A 418a), the judge denied defendant's motion. (A 15)

2. Motion for a continuance.

On January 2, 1975, the defendant discovered for the first time, through the government's requests to charge, that the prosecutor intended to prove alleged "similar acts" to establish willfulness.

Defendant's counsel promptly asked the nature of the similar acts, since, as he told the court at the time:

> "I, frankly, am in no position whatever to defend Mr. Leonard in connection with those similar acts because I have no idea what they are." (A 310a)

The Court declined to order the government to supply the defendant with either a bill of particulars or a list of "similar act" witnesses, but did "suggest that the government, having the *Baum* [*U.S.* v. *Baum*, 482 F.2d 1325 (2nd Cir. 1973)] case in mind, . . . make its own determination" as to whether it should make disclosure. (A 444a)

Trial was scheduled to begin on Monday, January 13, 1975. On Friday afternoon, January 10th, the government

delivered to defense counsel copies of Chase Manhattan Bank ("Chase") checks totalling $383,000 which had been paid to Leonard in 1968 allegedly at the direction of a Swiss bank. The apparent purpose of this evidence was to show circumstantially the falsity of an affidavit Leonard had signed in 1969 denying he had a foreign bank account.*

On the following Monday, the day trial was to begin, defendant's counsel notified the Court that these checks came as a total surprise to him, that he was "in no position to defend that charge" and that he requested a continuance to meet this proof:

> "I invited Mr. MacDonald to give some particulars and your Honor ordered him to do so and they came on the eve of trial. I think that checks, which are six or seven times or eight times as much as is charged in the indictment, is about as much from left field as you can imagine, as your Honor spoke about coming from left field.
>
> I think the prejudice in these checks far outweighs the probative value that they have.
>
> I submit the Government is attempting to introduce them merely to inflame the jury that Mr. Leonard received many checks during 1968.
>
> I believe [the prosecutor] will not be able to establish or even to allege that these checks constituted income." (A 8)

However, the Court declined to grant the continuance, but without prejudice to defendant's right to renew the motion during the trial. (A 10-11)

3. Motion to prevent the government from interfering with defendant's interviews of prospective witnesses.

Prior to trial, defendant's counsel sought to interview several of the government's prospective witnesses. The

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* This affidavit is discussed more fully in Point III, *infra*.

prosecutor insisted (over the defendant's objection) on being present during these interviews, which were recorded by a stenographer (A 79a-251a, 452a-545a), and on numerous occasions instructed the witnesses not to answer certain of the questions asked by defendant's counsel.

Defendant moved to obtain orders compelling the witnesses to answer the challenged questions and directing the government not to interfere with defendant's pre-trial preparations. The Court denied defendant's motion. (A 353a-354a)

The Trial

The Government's proof fell into two categories: evidence relating to the specific crime with which Leonard was charged and evidence relating to alleged similar acts, i.e., secret Swiss bank accounts. The thrust of the government's case on the charges in the indictment was that Leonard had received and cashed checks from Treadwell totalling $24,168 in 1967 and $58,648 in 1968, which he did not report in his tax returns for those years. Unlike most cases where the major portion of the evidence relates to the specific charges in the indictment, and only a small part to alleged similar acts, here the bulk of the government's proof pertained to the alleged Swiss accounts.

The Government's Case

1. The Union Carbide Contract.

Henry Mitchell, a UCC employee, testified that in February 1967, UCC entered into a contract with Leonard, who was then doing business as Leonard Process. (A 89) The UCC contract provided that Leonard was to design two large chemical alkyl-amine plants for UCC, one in Taft, Louisiana and the other in South Charleston, West Virginia. Leonard, Mitchell stated, was the only person who both possessed and was willing to sell the technology necessary for the construction of what was to be the largest amine plant in the world. (A 112) The amine plant

Leonard designed in Taft, Louisiana, was a complete success; it was built on time and within the allotted budget of $7,000,000. (A 111, 112, 135)

The UCC contract originally provided that Leonard was to receive a fixed fee of $750,000 (plus expenses) payable in installments of $37,000 each plus various lump sum payments.*

The UCC contract also provided that Leonard was to receive a 10% override (based on costs of $850,000) for supervising certain detailed engineering work which Leonard sub-contracted to Treadwell. The override was payable by Treadwell after Treadwell received payment from UCC. (GX 3) However, the contract was amended when UCC decided not to build the West Virginia plant and Leonard's 10% override fee was eliminated as there was no detailed engineering performed by Treadwell on the South Charleston plant. (A 98)

UCC's payment procedure for the engineering work was to forward to Leonard checks in payment of Treadwell's invoices plus 10%. Leonard endorsed the checks over to Treadwell, which in turn remitted to him its own check for his 10% override. These Treadwell checks, which were cashed, totalled $24,168 in 1967 and $58,648 in 1968. (GX 44-48, 50-63)

On February 1, 1968, with UCC's consent, Leonard transferred Leonard Process' assets, including the UCC contract, to Leonard Corp., a wholly owned Subchapter S (tax-option) corporation. (A 98-99) (GX 65) The government proved that Leonard diverted $52,455.22 in Treadwell checks from Leonard Corp. (GX 54-63)

Notwithstanding Leonard's diversion of these monies, they were still income of Leonard Corp. and reportable

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* All of the $750,000 was included either in Leonard's personal tax returns for 1967 and 1968 or in Leonard Corp.'s tax return for fiscal 1968. The government claimed, however, that Leonard delayed reporting until 1968 four $37,000 checks paid during 1967. (GX 1, GX 2, DX G)

by the corporation. They were taxable to Leonard, and reportable by him, only to the extent of Leonard Corp.'s earnings. Since the corporation had no earnings (GX 87, DX X & Y), the diverted funds constituted a constructive return of capital and were not taxable to Leonard.

2. Leonard's 1967 and 1968 tax returns.

Tax returns filed in Leonard's name for the years 1967 and 1968 reflected the following:

1967 (GX 1)

Schedule C [Sole Proprietorship]		
Gross Receipts	$461,000.00	
Net Income	256,873.95	
Total Income (Adjusted Gross Income)	259,051.95	
Tax (before credits)		$82,056.40

1968 (GX 2)

Schedule C [Sole Proprietorship]		
Gross Receipts	$142,000.00	
Net Income	114,726.00	
Total Income (Adjusted Gross Income)	134,276.00	
Tax (before credit)		$28,926.77

The only witness to testify about the preparation of the 1967 return was Marion Bardes, an independent accountant who did free-lance work for defendant's accounting firm, Leskowicz, Brower & Driver. (A 446) In the summer of 1968 she prepared certain schedules for a financial statement for Leonard Process, based on Leonard's bank statements from First National City Bank. (A 418, 422, 426)

On cross-examination, however, it was revealed that she had not actually prepared the defendant's 1967 return:

> "Q. Were you the person who prepared the 1967 income tax returns for Mr. Leonard?

A. Personal return?
Q. Yes, ma'am.
A. No, sir." (A 430)

While she did prepare a penciled copy of the first page of a draft of the 1967 return (GX 92), this draft varied materially from the return Leonard actually filed. (A 431) (Compare GX 1 and GX 92) Most importantly, however, she could not recall where she had gotten the figures that did appear on her draft:

"Q. Could you tell us where you got the information to put the numbers on that [penciled] return?
A. Honestly, I can't tell you. I would assume that I got them through Mr. Leskowicz." (A 432)

The work Miss Bardes did was primarily related to the preparation of financial statements for Leonard Process, which were completed on or about July 2, 1968, when they were verified by a letter from the Leskowicz, Brower & Driver firm to Leonard. (DX S) This was after Leonard's return had been filed. (A 438) No witness, therefore, connected the 1967 return (GX 1) either with Leonard or his books and records.

Emil Nothofer, another accountant employed by the Leskowicz firm, (A 450) testified that he prepared Leonard's 1968 return (GX 2) from material supplied to him by Leskowicz. (A 455) The government did not call Leskowicz on its direct case.

Leonard's 1968 return showed defendant had overpaid his 1968 taxes by $15,000 and was entitled to a refund. (GX 2) The return was filed at the IRS office in Philadelphia, Pennsylvania, which was the proper place at that time for a New Jersey resident (such as Leonard) to file. (A 463)

There was no testimony during the government's direct case as to whether Leonard had actually signed either his 1967 or 1968 return.

3. The Audit.

Revenue Agent Laski (who as noted previously was assigned to the FBA project and eventually became the project leader) testified that in 1968, as part of his investigation of Leonard's tax return, he contacted Edward Leskowicz, a certified public accountant, whose firm, Leskowicz, Brower & Driver, appeared on Leonard's 1967 return. (A 297)

Laski conducted the audit at Leskowicz's office. At the outset, Laski asked Leskowicz for a number of documents, including the UCC contract and various UCC invoices. (A 297-298) Leskowicz told Laski that he had not prepared the 1967 tax return. (A 301) There was apparently a delay in Leskowicz's producing some of the invoices, (A 303) but they were eventually produced. (A 298-304)

Leskowicz also produced a copy of the UCC contract (GX 66) in which the clause relating to payments of the 10% Treadwell override to Leonard had been crossed out.*

Laski claimed that he met with Leonard and Leskowicz at Leonard's office in March 1969, and that Leonard said at that time that this provision in the UCC contract had been altered. (A 207) Mitchell, however, denied that there had been any changes in the provision relating to Leonard's right to receive a 10% override from Treadwell, and said that the initials near the crossed-out portion of the contract were not his. (A 177)**

Laski testified that he had been unaware of the assignment of the UCC contract to Leonard Corp. (A 355)

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* Although the contract offered by the government at trial (GX 66) had initials next to the crossouts, (which were apparently related to the elimination of the engineering work on the South Charleston plant), Laski maintained that the initials were not on the contract he had originally seen. (A 312)

** There was also some evidence introduced by the government that four invoices from Leonard's company in 1967 for four $37,000 payments from UCC had been altered to reflect a 1968 billing date. Leonard had deposited these four checks in 1968 and they were included either on his Schedule C for that year or in Leonard Corp.'s tax return. (GX 2, DX Y)

Leonard Corp.'s fiscal 1968 tax return was prepared by Leskowicz, Brower & Driver, (A 466) but the accountants neglected to file it although they had a signed copy of an amended return in their file. (DX X and Y)* It, as well as Leonard Corp.'s books and records (GX 87), shows that the corporation lost over $73,000 in fiscal 1968.

4. The Swiss bank affidavit.

Laski claimed his only meeting with Leonard had occurred on either March 17 or 18, 1969, (A 310) and that he sought the meeting to find out whether Leonard had a Swiss bank account. (A 337) He conceded that he had found no indication of a Swiss bank account during his audit even though he had spent over 250 hours reviewing Leonard's records. (A 282) At this meeting, Laski gave Leonard no constitutional warnings and did not inform him of the criminal nature of the investigation. (A 418a) According to Laski, Leonard denied that he presently had a foreign account. (A 207)

Thereafter, at the direction of his superiors, Laski dictated an affidavit for Leonard to sign. Sometime later, Leskowicz returned it, bearing the defendant's signature. (A 212)

The affidavit dictated by Laski was substantially broader than and different from the defendant's oral denial. More particularly, the Laski-dictated affidavit stated:

(1) "I do not now and *I have not had any foreign* bank accounts"; and

(2) "*I have not had any transactions or dealings of any nature with any foreign banks or other representatives* except for (specified loans in Australia and currency conversions)". (Emphasis added) (GX 74)

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* The court admitted the corporate return in evidence but only for the limited purpose of showing that it was prepared by the Leskowicz firm. (A 472-473)

Leonard had not told Laski that he had *never* had a foreign account. Leonard had only denied "having" a foreign account. (A 207) Further, Leonard did not tell Laski that he had never had any transactions or dealings with a foreign bank or representative. (A 207) Yet Laski dictated an affidavit for Leonard to sign that contained factual assertions Leonard had never made to him. The government did not call Leskowicz or offer any proof as to how the defendant's signature came to appear on the affidavit or, more importantly, even whether he had read it before signing or merely assumed that it incorporated what he had told Laski.

The government sought to prove the falsity of the Swiss bank affidavit through the testimony of Harris Egan, the manager of a branch office of Chase Manhattan. (A 479) He stated that between April and November of 1968 he delivered Chase checks totalling $383,000* to defendant. (A 489) (GX 81)

Egan testified that Chase's record of the transfer and the identity of the transferor was contained on a "fan-fold form" (A 482) which had been destroyed in the normal course of the bank's business in 1973 and was therefore unavailable at trial. (A 483)

Carbons of the checks, as well as the checks themselves, were produced. (GX 81) On each carbon was the notation "Notify and Pay" which, Egan stated, meant that the branch had been notified and authorized by Chase's main office to pay the money to the payee. (A 484) Three of the carbons (which Leonard never saw) also included the additional notation "H/O Int'l" which, according to Egan, meant "Head Office International". (A 484) Chase's international office handled money coming from overseas banks. (A 484)

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* The checks were in the following amounts: (GX 81)

April 12, 1968	$ 25,000	September 12, 1968	$ 64,000
April 12, 1968	$ 20,000	September 12, 1968	$ 16,000
April 26, 1968	$120,000	November 27, 1968	$138,000

With considerable prodding from the prosecutor, and over defendant's objection to this testimony, Egan testified from memory as to the contents of the destroyed fanfold forms which he had last seen seven years before:

> "Q. Can you tell the jury your best recollection, please, of what that notation was?
>
> A. Yes. These monies were all payable to Mr. Jackson D. Leonard and these monies came in through a Swiss bank and they came in through the same Swiss bank, through the same channels each time. Past that, I have no recollection of the bank in question. I couldn't be certain.
>
> Q. What about the remitter? What is your best recollection with respect to what the fanfold form said in that respect?
>
> A. My best recollection on that is that these came through a numbered account." (A 486)

The carbon of one of the checks contained a notation "Rec'd from: Banque Continental de Zurich". However, in proceeding with his questions, the prosecutor changed the name from "Banque Continental" to "Banque Cantonale" (which may have been a bank name disclosed by the mail watch); thereafter the witness kept referring to Banque Cantonale:

> "Q. Do you happen to know that there is a bank known as Banque Cantonale, in Zurich?
>
> A. Yes, there is.
>
> Q. Does that refresh your recollection with regard to the original notations to the fanfold forms you described?
>
> A. My best recollection would be Banque Cantonale in Zurich, on that." (A 488)

Despite the fact that the Swiss bank affidavit did not purport to address itself to *indirect* transactions and despite the fact that the IRS drafted the affidavit, the government contended that the payments by Chase constituted "indirect" dealings with a foreign bank which

rendered the affidavit false and made it proper evidence of a similar crime relevant to willfulness. (A 497)

5. Eva Brooke's testimony.

Eva Brooke, the widow of an employee of Kerr-McGee Chemical Corporation (A 509) testified that in the summer of 1971 (three years after the last tax-return year in the indictment) she was present when the defendant had business discussions with her deceased husband. (A 510) According to Mrs. Brooke, "Mr. Leonard was extremely anxious that my husband join him in business" (A 510) and as a result offered him:

> "A free apartment at Sutton Place, and he mentioned the sum of $100,000 a year, with my husband as president of the company, 50,000 of which would be made in U.S. dollars and 50,000 to be deposited into a Swiss bank account." (A 510-511)

Mrs. Brooke also claimed that there was "a written note on this, but I did not see it myself." (A 511) During the evening, Leonard and his wife and Mr. and Mrs. Brooke went to dinner and then to P.J. Clarke's for drinks. (A 886) Mrs. Brooke stated that some time during that evening there was discussion as to how to open a Swiss bank account and Leonard said: "I have one." (A 511)

Mrs. Brooke also said she questioned Leonard about Swiss banks, and Leonard mentioned that "Swiss bank accounts are numbered and not in a name." (A 512)

The government claimed that Eva Brooke's testimony was evidence that Leonard had made a false statement in his 1971 return when he checked the box that indicated that he did not personally have "any interest in or signature or other authority over a bank account in a foreign country." (GX 83) As we show below, the government failed to prove that the account which Leonard allegedly stated he had was a personal rather than a corporate account.

The Defendant's Case

Since the government had contended, relying on the statutory presumption (26 U.S.C. § 6064*), that Leonard had signed his 1967 and 1968 returns**, Pearl L. Tytell, a handwriting expert, testified that the defendant had not signed the 1968 tax return and that the person who signed the return for Leskowicz, Brower & Driver (Leonard's accountants) had signed not only Leonard's signature but his wife's signature as well. (A 628-629) She further testified that the signature on the 1967 return was so smudged that she could not venture an opinion as to who had signed it.*** (A 662)

Teresa Daniti, secretary of Leonard Corp., and custodian of its records, produced expense reports that established that Leonard was in Australia on March 17 and 18, 1969, (A 607-608) (DX AA, AB, AC, AD) the dates Laski testified he met with Leonard, and defendant, according to Laski, allegedly falsely denied having a foreign bank account. (A 207, 310)

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* Reprinted in the Addendum to this brief at p. 1.

** The government's reliance on the theory that the defendant had personally subscribed to the returns was expressly stated in its opening (A 20-30), the indictment, and its requests to charge. (A 5a, 67a) However, the trial court pointed out at a conference just after the completion of the government's case that it appeared, at least to the court, that the same person had signed the accountant's name, the defendant's name and his wife's name to the 1968 return. (A 587)

*** This testimony was given almost in its entirety on Friday afternoon, January 17, 1975. Before the government was required to cross-examine, the trial was adjourned for the weekend. Saturday, January 18, 1975, the government called Leskowicz to the U.S. Attorney's office (A 710) and asked him for the *first* time who had signed the 1968 return. The Saturday interview of Leskowicz lasted 3 hours. (A 731) Leskowicz was then called the following Monday, January 20th, and he testified that he had signed the return but that defendant had authorized him to do so and had also authorized him to sign his wife's name (A 701) even though the defendant concededly never saw the return before it was filed. (A 718)

The Government's Rebuttal

Edward Leskowicz, the defendant's former accountant, was called in rebuttal by the government. He admitted that he had signed not only his firm's name on Leonard's 1968 return, but also both Leonard's and his wife's signature as well. (A 701)

Notwithstanding his earlier statement to defendant's counsel during an interview on January 2, 1975 that he could not recall these events (A 704), Leskowicz claimed that on August 14, 1969, a day before the return was required to be filed, Leonard and he had a telephone conversation in which Leonard orally authorized him to sign the return on his behalf and on behalf of his wife. (A 701)

Most importantly, however, Leskowicz stated that Leonard never saw the 1968 return before it was mailed (A 718) and further that his firm sent the return directly to the IRS. (A 701) He also admitted that he did not have a written power of attorney from Leonard and never made any effort to get one. (A 723)

Leskowicz related that in the course of the tax audit he had contact with perhaps as many as 17 different IRS agents. (A 707-708) However, not one government representative asked him who signed the 1968 return until after defendant 's handwritting expert had testified that Leonard had not signed the return. (A 707)

Summation and Charge

In order to avoid repetition, the portion of the charge and summation to which defendant objects will be set forth in the argument.

Motion for a New Trial

Following conviction, defendant moved in the alternative for a judgment of acquittal and a new trial. The grounds for the motion were: (1) the impropriety of the mail

watch; (2) the failure of the IRS to give Leonard timely constitutional warnings; (3) the improper admission of similar act evidence; (4) the government's interference with defendant's interviews of prospective witnesses; (5) the insufficiency of the evidence; (6) the inaccuracy of the testimony before the grand jury; and (7) the prejudicial nature of the prosecutor's opening statement.

These grounds are all discussed in detail in the arguments which follow.

ARGUMENT

POINT I

The Court below erred when it declined to suppress evidence obtained as a result of the failure of IRS Agent Laski to warn Leonard of his constitutional rights as required by IRS regulations governing the conduct of criminal tax fraud investigations.

This case squarely presents the issue of whether an IRS agent conducting a criminal investigation is required to warn a taxpayer of his constitutional rights. The First and Fourth Circuits have already held that since recent IRS rules require IRS agents to give full constitutional warnings to taxpayers suspected of criminal tax fraud, any documents or information obtained in violation of such rules will be suppressed. *U.S.* v. *Leahey,* 434 F.2d 7 (1st Cir. 1970) and *U.S.* v. *Heffner,* 420 F.2d 809 (4th Cir. 1970).

A. The IRS must give full constitutional warnings to taxpayers who are subjects of criminal investigations.

Although this Court has held that warnings are not constitutionally required with respect to non-custodial questioning by the IRS, *U.S.* v. *Caiello,* 420 F.2d 471 (2nd Cir. 1969), *cert. denied,* 397 U.S. 1039 (1970), *U.S.* v. *White,* 417 F.2d 89 (2nd Cir. 1969), *cert. denied,* 397 U.S. 912 (1970) and *U.S.* v. *Squeri,* 398 F.2d 785 (2nd Cir. 1968), this Court has not yet considered the effect of two recent IRS news releases which set forth self-imposed obligations to advise taxpayers that they are under investigation for criminal

tax violations. It was these two news releases that were held by the First and Fourth Circuits to be binding on the IRS. *U.S.* v. *Leahey, supra* and *U.S.* v. *Heffner, supra.*

Internal Revenue Service News Release No. 897, issued October 3, 1967, provides:

> "In response to a number of inquiries the Internal Revenue Service today described its procedures for protecting the Constitutional rights of persons suspected of criminal tax fraud, during all phases of its investigations.
>
> Investigation of suspected criminal tax fraud is conducted by Special Agents of the IRS Intelligence Division. This function differs from the work of Revenue Agents and Tax Technicians who examine returns to determine the correct tax liability.
>
> Instructions issued to IRS Special Agents go beyond most legal requirements to assure that persons are advised of their Constitutional rights.
>
> On initial contact with a taxpayer, IRS Special Agents are instructed to produce their credentials and state: 'As a special agent, I have the function of investigating the possibility of criminal tax fraud'.
>
> If the potential criminal aspects of the matter are not resolved by preliminary inquiries and further investigations become necessary, the Special Agent is required to advise the taxpayer of his Constitutional rights to remain silent and to retain counsel.
>
> If it becomes necessary to take a person into custody, Special Agents must give a comprehensive statement of rights before any interrogation. This statement warns a person in custody that he may remain silent and that anything he says may be used against him. He is also told that he has the right to consult or have present his own counsel before making a statement or answering any questions and that if he cannot afford counsel he can have one appointed by the U.S. Commissioner.

> IRS said although many Special Agents had in the past advised persons, not in custody, of their privilege to remain silent and retain counsel, the recently adopted procedures insure uniformity in protecting the Constitutional rights of all persons."
>
> (reprinted in 1967 CCH Fed. Tax Rep. ¶ 6832).

Internal Revenue Service News Release No. 949, issued November 26, 1968, further provides:

> "One function of a Special Agent is to investigate possible criminal violations of Internal Revenue laws. At the initial meeting with a taxpayer, a Special Agent is now required to identify himself, describe his function, and advise the taxpayer that anything he says may be used against him. The Special Agent will also tell the taxpayer that he cannot be compelled to incriminate himself by answering any questions or producing any documents, and that he has the right to seek the assistance of an attorney before responding."
>
> (reprinted in 1968 CCH Fed. Tax Rep. ¶ 6946 and 1969 P-H Taxes, ¶ 55, 467).

Since the date these news releases were issued, the First and Fourth Circuits, both of which had previously held that constitutional warnings were not required, have revised their positions.*

U.S. v. *Heffner, supra,* was the first appellate decision to hold that IRS agents must comply with the procedures set forth in the aforesaid news releases. The Court's analysis of the issue merits extensive quotation:

> ". . . voluntarily, IRS took upon itself the obligation to give taxpayers, before interrogation, notice that they were suspected of criminal tax fraud and the

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* All the previously cited Second Circuit cases dealt with evidence or admissions obtained prior to October 3, 1967, the date IRS News Release No. 897 was issued.

> further obligation to give the full *Miranda* warnings before seeking incriminating statements.
>
> * * *
>
> An agency of the government must scrupulously observe rules, regulations, or procedures which it has established. When it fails to do so, its action cannot stand and courts will strike it down . . .
>
> * * *
>
> It is of no significance that the procedures or instructions which the IRS has established are more generous than the Constitution requires . . .
>
> * * *
>
> Nor does it matter that these IRS instructions to Special Agents were not promulgated in something formally labeled a 'Regulation' or adopted with strict regard to the Administrative Procedure Act . . ."
>
> (420 F.2d at 811, 812) (citations omitted)

Similarly, in *U.S.* v. *Leahey, supra,* the First Circuit affirmed a decision by the trial judge suppressing information, books and records obtained from a taxpayer by Special Agents who failed to give the taxpayer the warnings required by the news releases:

> "The crucial question is whether we must exclude this evidence so that agencies will be compelled to adhere to the standards of behavior that they have formally and purposely adopted in the light of the requirements of the Constitution, even though these standards may go somewhat further than the Constitution requires.
>
> * * *
>
> . . . the Court in *Miranda,* as we have noted, specifically asked law enforcement agencies to develop better ways of harmonizing the protection of individual rights with efficient enforcement of the law. The

> Service has tried to do this. We must assume that the publicly announced procedure was arrived at only after painstaking intra-agency assessment. Were we to say that *Miranda* is the ceiling rather than the floor of the rights of citizens vis-a-vis the government, we would make a mockery of the *Miranda* invitation.
>
> . . . the I.R.S. press release was deliberately in response to 'a number of inquiries' and avowedly for the purpose of 'protecting the Constitutional rights of persons suspected of criminal tax fraud'. When an agency 'goes public' it does not do so lightly. Its obligations increase just as do those of a private corporation. . . .
>
> * * *
>
> It is important here that the procedure set forth in the news release was an agency wide directive designed to protect taxpayers by setting a clear and uniform standard governing the first contact between a Special Agent and a tax fraud suspect." 434 F.2d at 10-11.

The Court in *Leahey* concluded that due process requires that the IRS follow its announced procedures:

> "Here, however, we have the two factors intersecting: (1) a general guideline deliberately devised, aiming at accomplishing uniform conduct of officials which affects the post-offense conduct of citizens involved in a criminal investigation; and (2) an equally deliberate public announcement, made in response to inquiries, on which many taxpayers and their advisors could reasonably and expectably rely. Under these circumstances we hold that the agency had a duty to conform to its procedure, that citizens have a right to rely on conformance, and that the courts must enforce both the right and duty." *Id.* at 11.

It is respectfully submitted that this Court should follow the First and Fourth Circuits in requiring the IRS

to comply with its own rules of conduct in criminal investigations.*

Such a decision would be consistent with the strong public policy, clearly expressed by the Supreme Court in *Yellin* v. *U.S.*, 374 U.S. 109 (1963), *Vitarelli* v. *Seaton*, 359 U.S. 535 (1959), *Service* v. *Dulles*, 354 U.S. 363 (1957), and *U.S. ex rel. Accardi* v. *Shaughnessy*, 347 U.S. 260 (1954) that arbitrary deviations from published procedures should not be permitted. See also, *Donham* v. *Resor*, 436 F.2d 751 (2nd Cir. 1971), *Smith* v. *Resor*, 406 F.2d 141 (2nd Cir. 1969) and *Hammond* v. *Lenfest*, 398 F.2d 705 (2nd Cir. 1968).

B. Leonard was the subject of a criminal investigation.

The record clearly shows that Laski was assigned to audit Leonard's returns because of (1) an allegation by an informant that Leonard was receiving commercial bribes in connection with the UCC contract (GX 3) or (2) the discovery of information, obtained through the FBA mail watch, that Leonard either had a secret Swiss bank account or had financial dealings of a regular nature with Swiss banks, although his tax returns failed to reflect any Swiss transactions or income. (GX 1, GX 2, DX E) (A 334a)

Specific information from an informant that a taxpayer is receiving commercial bribes from a named corporation clearly constitutes an allegation of criminal conduct. An investigation of whether the taxpayer is in fact receiving illegal kickbacks where his tax returns do not disclose such payments is, as Judge Owen remarked below, "prima facie criminal".** (A 336-337a)

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* The Fifth Circuit has also ruled that the IRS must comply with the procedures outlined in the IRS news releases, but that substantial, rather than literal, compliance is sufficient. *U.S.* v. *Mathews*, 464 F.2d 1268 (5th Cir. 1972.)

In the present case, IRS Agent Laski gave no constitutional warnings and, in effect, acted as "a Trojan horse bearing criminal investigators". *U.S.* v. *Bembridge*, 458 F.2d 1262 (1st Cir. 1972).

** Indeed, informant allegations of criminal conduct were generally assigned to Special Agents to investigate and were only "farmed out" to Revenue Agents because of insufficient manpower. (A 415a)

At the pretrial hearing below, the government contended that the FBA project was essentially civil in nature. (A 355a-367a, 407a)

The government called only one witness, Revenue Agent Morris, to testify about the project. Morris, who jointly with Special Agent Hyman Boller, had supervised the project,* claimed that it was designed merely to develop routine "audit techniques", "to investigate the use of foreign bank accounts by United States tax payers and to see what [the IRS] could do to come up with some means of coping with the problem which at that time was increasing." (A 356a) The "problem" Morris referred to was obviously the commission of tax fraud through the use of foreign bank accounts.

The testimony at the hearing disclosed that the FBA investigation was approved by the Director of Intelligence and was initially handled and directed exclusively by Spe-

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*The court refused to permit Leonard to subpoena Special Agent Hyman Boller, the other member of the task force, who was in charge of the Intelligence Division's part of the project, thereby depriving the defendant of the opportunity to prove that the FBA project was an Intelligence operation designed to ferret out criminal tax fraud. (CX 1, A 442a) Defendant was also not allowed to show, through interrogation of the Special Agents who actually conducted the mail watch, that the IRS's interference with normal mail distribution procedures caused substantial delays in the delivery of the mail in violation of 18 U.S.C. § 1701. Cf. *U.S.* v. *Costello*, 255 F.2d 876 (2nd Cir. 1958), *aff'd*, 350 U.S. 359 (1956). See also *U.S.* v. *Isaacs*, 347 F. Supp. 743 (N.D. Ill. 1972), where the court granted defendant's motion to compel the government to state, for the defendant's use:

> "(1) the full extent and duration of the mail covers; (2) the circumstances under which it was instituted, including the names and positions of all persons who authorized it; (3) the procedure by which it was instituted, including the names and positions of all persons involved therein; (4) the purported justification for its institution; (5) the information it produced; (6) the names and positions of all persons to whom such information was transmitted and the date of such transmission; (7) the use made of such information." *Id.* at 750.

The court also quashed subpoenas duces tecum served by the defendant on various IRS officials involved in the FBA project mail watch. (A 15)

cial Agents, the IRS's criminal investigators. (A 396a) The defendant offered to prove that the project began with Special Agents writing to Swiss banks and posing as Americans who claimed to be interested in opening Swiss bank accounts.* The envelopes containing the banks' replies, mailed (as is the practice) without return addresses, bore metered stamps with numbers which varied depending on the bank. By compiling a master list of these meter numbers, the IRS was able to identify mail from specific Swiss banks. (A 376a)

The Special Agents thereafter conducted a mail watch or mail cover of all mail arriving at JFK International Airport from Switzerland. (A 375a-381a) The mechanics of the operation were handled by Special Agents who intercepted, inspected and microfilmed the mail.

The then current Post Office regulations demonstrate that the mail watch was part of a criminal investigation. *Postal Bulletin* 20478; Part 861 of the *Postal Manual* of the Post Office Department. See Addendum p. 2 *et seq.*

Parts 861.42b and 861.51a of the Post Office regulations provided as of 1968 and 1969, when the IRS mail cover was conducted, that mail watches could be authorized only by a limited number of highranking members of the Post Office Department and would be instituted at the instance of law enforcement agencies only when the requesting authority stated in writing grounds sufficient to demonstrate that the mail cover (1) was essential for the national security, (2) would help locate a fugitive, or (3) would assist in obtaining information concerning "*the commission or attempted commission of a crime.*" [Emphasis added].

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* However, the court refused the defendant permission to do so. (A 15) The writing of such letters to Switzerland for the purpose of clandestinely uncovering the identity of Swiss bank account holders may very well have violated Swiss bank secrecy and the Swiss Economic Espionage Act, as well as the Swiss-American Tax Treaty, see CX 1. The court refused to permit the defendant to establish these alleged violations. (A 15)

Therefore, in order to obtain Post Office approval for the FBA mail watch, the IRS, and in particular the Intelligence Division, was required to specify *in writing** "the reasonable grounds that exist which demonstrate the mail cover is necessary to *obtain information regarding the commission or attempted commission of a crime*". [Emphasis added] If the IRS did not do so, the mail watch violated postal regulations. If the IRS in fact supplied the Post Office Department with a formal request, the only ground it could have specified was that the FBA project was a criminal investigation.**

Further, the IRS Revenue Agent Manual prohibits "Audit Division" personnel (including Revenue Agents) from requesting mail covers in connection with the examination of tax returns *"or for any other purpose"*. "Mail covers" can only be instituted through the Chief of Intelligence and then only in *"limited . . .* types of cases", i.e., criminal investigations (DXH B).

Additionally, the manner in which the investigation was run clearly demonstrates that the project was essentially criminal. First of all, it was highly secret. Agents assigned to the project were forbidden to reveal its existence to other IRS agents, except on a "need to know basis", hardly the characteristics of a routine civil project. (A 283) Moreover, the mail watch itself was conducted by Special Agents, who only handle criminal investigations.

Returns of taxpayers who the IRS determined were receiving mail from Swiss banks were pulled and examined by a task force which was co-directed by a Special Agent from the IRS's Intelligence Division. 110 "good candidates" for audit were then selected, apparently from those

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* Oral requests were permitted only where time was of the essence. However, the oral request had to be confirmed in writing within two business days, and no information could be released until the written request was received.

** The defendant was prevented from determining what the IRS actually did in this regard when the Trial Court quashed the defendant's subpoenas duces tecum. (A 15)

returns which reflected no Swiss bank account or transactions.

The techniques employed during these audits were those of criminal, not civil, investigations. For example, Revenue Agents were specially directed to scrutinize telephone records for telex and cable charges and the backs of checks for leads on Swiss accounts. (A 284) In addition, while trying to develop such leads, the Revenue Agents were specifically instructed not to reveal, in short to conceal from the taxpayer, the existence of information disclosed by the mail watch. (A 414a)

If such investigatory methods failed to establish independent proof of Swiss accounts, the Revenue Agent was generally instructed to confront the taxpayer directly and ask him point-blank (in a face-to-face meeting) whether he had any foreign bank accounts. (A 361a)

Where, as in the present case, the taxpayer was represented by an accountant, there was, of course, no legitimate audit purpose in seeking a face-to-face meeting. Realistically, the only reason why agents were instructed to speak to the taxpayer directly was so they could obtain either an admission of criminal conduct or a false denial, which itself would have constituted a violation of both 18 U.S.C. § 1001 and 26 U.S.C. § 7207, which make it a crime to give false statements to the IRS.

If the taxpayer denied the use of a foreign bank account, the Revenue Agent normally was directed to prepare an affidavit confirming the oral denial and to submit the affidavit to the taxpayer for his signature (A 362a), which is precisely what happened in the instant case. Indeed, the fact that the Revenue Agent insisted on an affidavit demonstrates that at this stage the "audit" was already focused on future court action.*

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* The insistence by a Revenue Agent that a taxpayer execute an affidavit is very rare; only in alimony cases (i.e., where alimony is

(*footnote continued on following page*)

Additionally, many of the taxpayers who were the subjects of these audits and who denied having a Swiss account were subpoenaed before grand juries in the Southern District of New York and questioned by Assistant U.S. Attorneys specifically on the existence of Swiss bank accounts, (A 371a) hardly the type of activity that would be necessary if the object of the project was developing civil "audit techniques". (A 407a)

Even Morris admitted, however, that the project had some criminal overtones. He conceded that the Intelligence Division's objective was "to develop Intelligence techniques. They are different." (A 407a)

Still further confirmation of the criminal nature of the FBA project was the continuation of the mail watch by Special Agents during the time when Revenue Agents were conducting the audits of the taxpayers suspected of maintaining Swiss accounts. (A 333a-334a)

C. Laski violated IRS rules when he failed to give Leonard constitutional warnings.

In the light of the foregoing, there can be no doubt that when Revenue Agent Laski, who was part of the FBA project, had his initial contact with Leonard, he was investigating allegations of criminal conduct, allegations made against Leonard first, by the undisclosed informant, and second, as a result of the FBA project itself. Laski was not auditing Leonard simply "to determine the correct tax liability".

Since Laski was conducting a criminal investigation, he was required to give Leonard constitutional warnings.

(footnote continued from preceding page)

deductible by the husband) and in certain estate cases are affidavits requested, but then the affidavits concern specific payments or items. (A 363a-364a) Here, by contrast, the affidavit did not focus on any specific amounts but merely documented the taxpayer's oral denial. Indeed, it was designed to force an admission out of taxpayers who would "think twice" before signing a denial. (362a, 370a)

In *U.S.* v. *Harary,* 70 Cr. 1104 (C.M.M.) (S.D.N.Y. 4/23/71), 71-1 USTC § 9362, Judge Metzner stated unequivocally that the standards of conduct set forth in the IRS news releases noted above apply to *Revenue Agents* (as well as to Special Agents) conducting non-custodial criminal investigations:

> "I agree with defendants that such regulations must be interpreted to apply to a Revenue Agent engaged in criminal non-custodial investigation." Id. at 86, 382.

The record is absolutely clear that Leonard was not warned that he was suspected of criminal activity nor that he could refuse to allow the IRS access to his books and records, until after he made incriminating statements and permitted the IRS to inspect his books and records. (A 418a) Consequently, this court should reverse Leonard's conviction and dismiss the indictment, since it was the product of illegally obtained evidence.

Alternatively, even should this court conclude that the FBA investigation was a civil, rather than a criminal, project (which the defendant emphatically does not concede), this court should nevertheless hold that Leonard should have been given constitutional warnings when Laski sought the Swiss bank affidavit since the only plausible reason for seeking a written denial of the Swiss account was to obtain evidence that could be used in a court of law either to convict Leonard of making false statements or to establish criminal willfulness in a tax fraud case.

At the very least, the court should suppress the Swiss bank affidavit and grant Leonard a new trial.

POINT II

The Court erred when it failed to dismiss the indictment or, alternatively, to suppress all evidence obtained as a result of an illegal mail watch.

Prior to trial, defendant moved, in the alternative, to dismiss the indictment or suppress evidence on the grounds that the indictment was based on, and the evidence obtained as a result of, an illegal mail watch.

A one day hearing was held on January 8, 1975 at which time the government called only one witness, Revenue Agent Bernard Morris.* Following the hearing, the court denied defendant's motion. (A 426a)

The mail watch was unlawful.

The mail watch conducted by the IRS violated Post Office Regulations and the Constitution, and may have also violated Swiss law.

Parts 861.42b and 861.51a of the Post Office regulations provided as of 1968 and 1969, when the IRS mail cover was conducted, that mail watches would be initiated at the instance of law enforcement agencies only when the requesting authority stated in writing grounds sufficient to demonstrate that the mail cover (1) was essential for the national security, (2) would help locate a fugitive, or (3) would assist in obtaining information concerning "the commission or attempted commission of a crime."**

Since the government did not offer in evidence any written request the IRS may have made to the Post Office seeking authorization for a mail cover, there is nothing in the record to show that the IRS complied with the requirement that it demonstrate in writing that reasonable grounds existed for the institution of a mail cover.

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* The court quashed the defendant's subpoenas duces tecum to the IRS for all documents relating to the mail watch. (A 15)

** This regulation was not known to defendant or cited to the court during the hearing on January 8, 1975, which took place on one day's notice.

Indeed, the record is barren of any evidence that there was any legitimate basis for requesting a mail watch. No proof was (or could have been) adduced that the mail cover was necessary to protect the national security or to apprehend fugitives. In fact, the only testimony as to the reasons for the mail watch was Revenue Agent Morris' comment that the IRS thought the project would help develop civil audit techniques relevant to foreign bank accounts.*

If this court accepts the government's contention below that the FBA project was a *civil* investigation, then, *ipso facto*, this court must hold that there was no legal justification for the mail watch under Part 861 of the Post Office regulations.

However, should this court agree with defendant that the FBA project was a criminal investigation, it still does not follow that the mail watch was properly authorized under the Post Office regulations.

The regulations do not authorize a "dragnet" approach to obtaining evidence of the commission of a crime.

Indeed, the language of the Regulations strongly indicates that the Post Office Department intended that only the mail of specifically identified individuals would be inspected. Thus Parts 861.42(a) and 861.51(a) both speak of having reason to believe that the "subject or subjects" of the mail watch are violating postal regulations. Similarly, Part 861.62 prohibits copying of information on envelopes mailed between the mail cover "subject" and his known attorney-at-law. 861.64 refers to mail covers ordered upon "subjects" engaged, or suspected to be engaged, in activities which jeopardize the national security, and 861.66 states:

> "Excepting fugitive cases [which of course concern specific known individuals], no mail cover shall remain in force when the *subject* has been indicted for any

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* See *supra*, Point I, page 31.

cause. If the *subject* is under investigation for further criminal investigations, a new mail cover order must be requested . . ." (Emphasis added)

Finally, 861.74 provides that the "subject" of a mail cover is entitled to discover any data relating to the mail cover.

Moreover, the mail watches which the courts have heretofore approved have all been quite limited in scope, and clearly restricted to the inspection of the mail sent to specific individuals who were reasonably suspected of having committed, or having attempted to commit, particular crimes. See, *e.g., Canaday* v. *U.S.*, 354 F.2d 849 (8th Cir. 1966), *U.S.* v. *Schwartz*, 283 F.2d 107 (3rd Cir. 1960), *cert. denied*, 364 U.S. 942 (1961), *U.S.* v. *Costello*, 255 F.2d 876 (2nd Cir. 1958), *aff'd*, 350 U.S. 359 (1956), and *U.S.* v. *Isaacs*, 347 F. Supp. 743 (N.D. Ill. 1972).

Here, in marked contrast, every envelope which came through Kennedy Airport from Switzerland and which lacked a return address was photocopied, and the name of the addressee recorded, (A 376-381a) irrespective of whether the IRS even had reason to believe it had been sent by a Swiss bank.

Even had the mail watch been restricted to mail sent by Swiss banks, it still would have been impermissibly broad. The mere fact that a person receives a communication from a Swiss bank does not establish probable cause for believing that he has committed or has attempted to commit a crime. This court can certainly take judicial notice that the vast majority of people who deal with Swiss banks have legitimate business transactions and therefore do not use Swiss accounts for illegal purposes.

Clearly, therefore, the FBA mail watch violated the applicable postal regulations.*

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* The regulations further provided explicit "limitations" on mail covers which clearly indicated a concern for a citizen's consti-

(*footnote continued on following page*)

The unlimited scope and duration of the mail watch also violated Leonard's First and Fourth Amendment rights.

The courts have long been sensitive to the importance in a free society of the privacy of the mail. As Justice Holmes aptly noted, ". . . the use of the mail is almost as much a part of free speech as the right to use our tongues . . .", *U.S. ex rel. Milwaukee Pub. Co.* v. *Burleson*, 255 U.S. 407, 437 (1921) (dissenting opinion), and, like free speech, the use of the mails is constitutionally protected. See *e.g., Lamont* v. *Postmaster General*, 381 U.S. 301 (1965).

Certainly, the Internal Revenue Service's inspection of all air-mail sent from Switzerland to the United States during the periods of January through April of both 1968 and 1969 cannot be said to have been carefully limited so as to cause the least possible interference with a recipient's rights. No effort was made to insure that the search would be restricted to seeking evidence of serious crimes. No probable cause was established or even asserted. No

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(*footnote continued from preceding page*)

tutional rights:

(1) "No person in the postal service . . . may break or permit breaking of the seal of any matter mailed as first class mail without a search warrant". [Fourth Amendment]

(2) "No mail covers shall include matter mailed between the mail cover subject and his known attorney-at-law". [Sixth Amendment]

(3) Except in national security and postal violation cases, "No mail cover shall remain in force for longer than 30 days" but "the requesting authority may be granted additional 30 day periods" under [certain conditions] but "No mail cover shall remain in force longer than 120 days" except on the personal approval of the Chief Postal Inspector" [First Amendment and Fourth Amendment] and

(4) "Excepting fugitive cases, no mail cover shall remain in force when the subject has been indicted for any cause." [Sixth Amendment and Due Process] Regulations Part 861.6.

The regulations also provided that "Any data concerning mail covers shall be made available to any mail cover subject in any legal proceeding through appropriate discovery procedures" and additionally all such data shall be retained for a period of eight years. Regulations Part 861.7.

judicial supervision was sought or exercised. No finding was made that less obtrusive means of obtaining evidence did not exist. No notice was given to the people whose mail was interrupted. Indeed, the Justice Department was not even consulted. (A403a-404a)

If the government is permitted to institute broadscale mail watches of entire classes of people without any showing that probable cause exists to believe they have committed or are about to commit specific crimes, the possibilities of abuse will be considerable. Compare, *U.S.* v. *Albarado*, 495 F.2d 799 (2nd Cir. 1974) and *U.S.* v. *Tortorello*, 480 F.2d 764 (2nd Cir. 1973), *cert. denied*, 414 U.S. 866 (1973).

There was present here no legitimate governmental interest which justified so broad-scale an invasion of privacy and infringement on freedom of speech and association. If the government has need of ascertaining whether taxpayers have dealings with Swiss banks, there are ways to do so that have far less adverse effect on the exercise of constitutional rights.*

Thus, while *Costello* upheld a limited mail watch of the mail sent to a specific person, the Court explicitly grounded its decision on the defendant's failure to show that the mail had been substantially delayed or that any laws had been violated. Here, however, the unlimited scope of the mail watch violated Post Office regulations and Leonard's First and Fourth Amendment rights,** and defendant has offered

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* See the Bank Secrecy Act of 1970, 12 U.S.C. §§ 1829b, 1951-1959, and 31 U.S.C. §§ 1051-1122.

** See also 18 U.S.C. § 1702 which provides in pertinent part as follows:

> "Whoever takes any letter, postal card or package . . . which has been in any Post Office . . . before it has been delivered to the person to whom it was directed, with design to obstruct the correspondence or to pry into the business or secrets of another . . . shall be fined not more than $2,000 or imprisoned not more than five years or both." See Addendum p. 1a.

to prove that the IRS's activities in seeking to discover the identity of the Swiss banks also violated Swiss law.*

Additionally, the government below never established that there had been no delay in the mail. The only witness called to testify, Revenue Agent Morris, had no personal knowledge of whether the defendant's mail was in fact delayed since he viewed the mail watch on only one occasion (A 396a). His hearsay testimony of what the IRS "sought" to do is not a sufficient substitute for direct proof of what actually occurred.

The illegal mail watch tainted the entire investigation of Leonard.

Wong Sun v. *U.S.*, 371 U.S. 471 (1963), prohibits the government from utilizing or exploiting illegally seized evidence (the "fruits of the poisonous tree") in criminal prosecutions. See also, *U.S.* v. *Edmons*, 432 F.2d 577 (2nd Cir. 1970) and *U.S.* v. *Lane*, 329 F.2d 848 (2nd Cir. 1964). Cf. *U.S.* v. *Cole*, 463 F.2d 163 (2nd Cir. 1972) and *U.S.* v. *Schipani*, 414 F.2d 1262 (2nd Cir. 1969), *cert. denied*, 397 U.S. 922 (1970).

Consequently, Leonard's conviction should be reversed and his indictment dismissed.

Alternatively, his conviction should be reversed and the evidence obtained as a result of the illegal mail watch should be suppressed.

The government cannot (and certainly did not) meet its burden of showing that it either would have obtained or did obtain the "similar act" evidence (described in detail in Point III *infra*) without the mail watch. The government had no "independent source" for obtaining this evidence; unlike *U.S.* v. *San Martin*, 469 F.2d 5 (2nd Cir. 1972) and *U.S.* v. *Falley*, 489 F.2d 33 (2nd Cir. 1973), it was not simply

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* Defendant offered to prove, through Bernard Reverdin, Esq., an expert on Swiss law, that the activities of the IRS in connection with the mail watch in Switzerland violated Swiss law. In particular, the defendant would have sought to prove that the efforts by IRS agents in Switzerland were designed to trick the Swiss banks into disclosing a means for identifying their account holders in violation of Swiss law. (CX 1) The court rejected defendant's offer of proof. (A 15) But Cf. *U.S.* v. *Toscanino*, 500 F.2d 267 (2nd Cir. 1974) where this Court condemned conduct by a U.S. law enforcement agency which violated foreign law.

"a question of time" before the government would have obtained it.

Indeed, the record is quite clear that as of the time that Laski sought an affidavit from Leonard denying having any foreign assets the IRS had been wholly unsuccessful in its efforts to corroborate its suspicion that defendant had a Swiss account and that its suspicion was based solely on information derived from the mail watch. See A 360-62a. Consequently, the Swiss bank affidavit was tainted by the illegal mail watch and at the very least, this evidence should be suppressed and Leonard granted a new trial. *Wong Sun, supra.* See also *U.S.* v. *Hearn*, 496 F.2d 236 (6th Cir. 1974)

POINT III

Leonard was convicted as a result of the improper admission of highly inflammatory and prejudicial evidence of crimes which were neither charged in the indictment nor proved at trial.

The indictment charged Leonard with making and subscribing tax returns which omitted specific items from his adjusted gross income for the years 1967 and 1968. He was not charged with income tax evasion, presumably because the government knew it would not be able to prove such a crime.

Nevertheless, under the guise of showing similar crimes relevant to willfulness, the government offered, and the court erroneously admitted, a massive quantity of evidence relating to Leonard's alleged ownership of secret Swiss bank accounts and alleged wide-scale evasions of income taxes, evidence wholly unrelated to the offenses charged in the indictment and specified in the government's bills of particulars.

As a consequence, the focus of the trial shifted from the charges in the indictment (whether Leonard had willfully subscribed tax returns which improperly omitted specific amounts) to the highly inflammatory and prejudicial allega-

tion that Leonard had a secret Swiss account. The result was that in reality Leonard was tried and convicted of having a Swiss account, rather than of failing to include certain items in his adjusted gross income in his 1967 and 1968 tax returns.*

A. The evidence of alleged similar crimes.

The government introduced evidence of two alleged "similar crimes" by Leonard as circumstantial evidence that when Leonard had committed the acts charged in the indictment, he had done so willfully. The first was executing an allegedly false affidavit in which the defendant denied having a Swiss account; the second was allegedly falsely stating in his 1971 tax return that he did not have signatory authority over a foreign bank account during 1971.

This Court has held that evidence of other crimes is admissible for any relevant purpose, including proof of willfulness. *U.S.* v. *Deaton,* 381 F.2d 114 (2nd Cir. 1967); *U.S.* v. *Crisona,* 416 F.2d 107 (2nd Cir. 1969). However, as the Court said in *Deaton,* such evidence is admissible only if its probative value outweighs its prejudicial effect, the prejudice being the danger that the jury is likely to conclude that because the defendant committed the similar crime, he is a "bad person" who deserves to be punished irrespective of whether the government has proved beyond a reasonable doubt that he has committed the crime charged in the indictment.

Whether the probative value of such evidence outweighs the prejudicial effect is a matter, in the first instance, for the trial judge's discretion. However, in the present case, as we show below, the trial judge merely deferred to the prosecutor's judgment, and did not, prior to its admission, make an independent determination of whether the similar-crime proof was admissible.

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* Only by reading the entire record, and in particular the prosecutor's opening and closing, is it possible to fully perceive the extent to which Leonard's trial revolved around the question of whether he had a Swiss account.

Moreover, the government never actually proved that Leonard's denials of having Swiss accounts were false. The evidence that was offered was not inconsistent with the challenged statements. Compare *Bronston* v. *U.S.*, 409 U.S. 352 (1973), discussed in detail, *infra.*

B. The trial court did not, prior to admitting the similar act evidence, exercise its discretion as to whether its probative value outweighed its prejudicial effect.*

Before the government's opening statement, the defendant advised the trial court that the government would offer proof which the government contended showed that Leonard had given the IRS a false affidavit and had a Swiss account from which he received hundreds of thousands of dollars.

The defendant requested the court to instruct the prosecutor not to mention the affidavit or alleged Swiss account. Rather than demand that the prosecutor present his "Swiss account" evidence outside the presence of the jury or even set forth his expected proof in detail before the government's witnesses testified so it could determine the admissibility of the Swiss account evidence, the trial court explicitly relied on the prosecutor's assurance that the government could establish that Leonard was guilty of similar acts:

> "The Court: Mr. MacDonald [Assistant U.S. Attorney] I am not prepared to say what you have in mind to support the use of that proof, and *I will at this point have to rely on your judgment that this is admissible,* because short of having in effect an advance run of it, I can't make the kind of judgment that would be definitive.

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* Despite the defendant's pretrial request, the trial court also never exercised its discretion to require the government under *U.S.* v. *Baum,* 482 F.2d 1325 (2nd Cir. 1973), to disclose the identity and nature of similar acts evidence prior to trial, but again deferred to the prosecutor with the caution that the government should, in light of the *Baum* case, consider making such disclosure. See *infra,* Point IV.

Mr. MacDonald: I just call the Court's attention to the xeroxes of the final check, which your Honor didn't have this morning, and that contains a recitation of the Swiss bank and that contains the source of the $138,000 paid, in Mr. Leonard's affidavit. That's not all—

The Court: You are going to establish by additional evidence that the defendant was aware that this was the case?

Mr. MacDonald: Yes, sir.

The Court: All right. Mr. Tigue [Defendant's attorney].

Mr. Tigue: Your Honor, I just want the record to be clear that I don't assent to any of this, and I want to make my position here." (Emphasis added) (A 18-19)*

C. The legal standard for proof of similar acts.

Although this Court has not yet ruled on the certainty with which similar act proof must be established in order for it to be admissible, other Circuits have concluded that the proof of the similar act must be "plain, clear and convincing". See, e.g., *U.S.* v. *Lawrance,* 480 F.2d 688 (5th Cir. 1973) and *Kraft* v. *U.S.,* 238 F.2d 794 (8th Cir. 1956); see also *McCormick on Evidence* (1954) § 157.

Defendant questions whether even the "plain, clear and convincing" standard is adequate to protect a defendant's presumption of innocence, but that is certainly the minimum standard that should govern proof of similar acts** and that minimum standard was not met in this case.

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* The court did make a subsequent determination after hearing the testimony that the evidence was admissible, but by then the damage had been done since the jury had already heard the testimony. (A 500)

** In order to convict a defendant, the prosecution has the duty of proving the defendant guilty beyond a reasonable doubt. Where the crime charged has a number of elements, each element must be so proved. *McCormick on Evidence* (1954) § 321.

(*footnote continued on following page*)

D. The Government never proved that Leonard had a Swiss account.

This case raises the precise problem faced by the Supreme Court in *Bronston* v. *U.S., supra,* where an alleged "false statement" was made during a bankruptcy hearing, in response to questions propounded by a creditor's lawyer:

> "Q. Do you have any bank accounts in Swiss banks, Mr. Bronston?
>
> A. No, sir.
>
> Q. Have you ever?
>
> A. *The company had an account there for about six months,* in Zurich.
>
> Q. *Have you any nominees* who have bank accounts in Swiss banks?
>
> A. No, sir.
>
> Q. Have you ever?
>
> A. No, sir." (409 U.S. at 354) (Emphasis added)

Bronston was prosecuted for perjury because he in fact *had* a personal Swiss account until shortly before the time he was questioned. The Supreme Court unanimously held, however, that since Bronston's answers were literally true —he never denied previously having had an account, he simply answered unresponsively with deliberate intent of misleading his questioner—he did not commit perjury.

If, as the Supreme Court held in *Bronston,* a witness does not commit perjury when his statements are literally

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(*footnote continued from preceding page*)

Leonard was indicted for subscribing false tax returns. To convict him of that crime, the government had to prove, beyond a reasonable doubt, that he knew the returns were false. If the necessary "willfulness" can be shown through the commission of "similar acts" which themselves need not be proved beyond a reasonable doubt, there is a serious anomaly in the law: in cases where the government lacks sufficient evidence to prosecute a suspect for committing a crime, it can call that crime a "similar act", establish its commission by a low standard of proof, and use the "fact" that the defendant committed that independent crime to prove that he is the type of person who a jury is entitled to believe would willfully commit the crime with which he is actually charged.

true (albeit unresponsive and even intended to mislead) so, too, a taxpayer who carefully makes a statement in such a way as to be strictly accurate, but not complete, cannot be viewed as having made a "false statement", which can be used to show criminal intent.

Indeed, there is even less justification for viewing Leonard's affidavit as a "false statement" than was the case in *Bronston*. In *Bronston*, the witness deliberately couched his reply in a misleading fashion; in contrast, Leonard merely signed an affidavit exactly as it was prepared by the government. (A 103a)

Leonard's allegedly false affidavit (which was dictated by IRS Agent Laski and was different from defendant's oral denial) stated:

(1) "I do not now and I have not had any foreign bank accounts"; and

(2) "I have not had any transactions or dealings of any nature with any foreign banks or other representatives except for (specified loans in Australia and currency conversions)". (GX 74)

The only evidence that even tends to show that this affidavit was inaccurate is testimony of Harris Egan, an officer of Chase Manhattan Bank who, some seven years earlier, received various phone calls and advices from the bank's main office in New York directing him to pay Leonard several installments aggregating $383,000. (A 479-504) Although the bank's records had been destroyed (A 482-483), thereby making it impossible for defendant's attorney effectively to cross-examine Egan, Egan recalled, after some prodding from the prosecutor, that these funds came through a numbered account at a Swiss bank. (A 485-486).

These transactions were "dealings" or "transactions" with Chase Manhattan. The checks which Egan delivered to Leonard stated on their face that they were "official" Chase checks. While the carbon copies of the checks reflected "H/O Int'l," Leonard never saw them. In short,

Leonard's only contact in these transactions was with an official of a domestic bank.

The government conceded in its summation that "[the affidavit] doesn't say anything about direct dealings with foreign banks or [even] indirect dealings with foreign banks".*

Further, there was no testimony or documentary evidence that the $383,000 came from a personal account of Leonard and the government offered no explanation as to the reasons for the payments. Indeed, as in *Bronston, supra,* the Swiss account could just as consistently have belonged to a corporation or third party as to Leonard personally.** As noted previously, Leonard had extensive dealings with foreign corporations in Europe. He designed chemical plants in Belgium, France, Italy and Germany. The transfers may well have been in relation to that work.*** Additionally, the affidavit (GX 74) itself revealed that Leonard made use of Australian banking facilities to secure a loan for a project in Australia and it is possible that he was repaid by the Australian corporation through a Swiss bank.

Leonard, who elected to exercise his privilege not to testify, was under no obligation to prove the alternative ex-

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* The government contended, however, that Leonard had an obligation to disclose any indirect transactions, although he was never asked about such transactions and the affidavit which the IRS prepared for his signature made no mention of them:

> "You may find that the instructions from the bank in Zurich make this affidavit false. He had dealings within the intendment of this affidavit with the bank in Zurich, and *he should have disclosed that* as *a . . . caveat* in his exceptions to the otherwise straight forward and unqualified statement." (A 949) (Emphasis added).

** Since the only Swiss bank that the mail watch disclosed had correspondence with Leonard was People Bank (DX E), it therefore would appear to be extremely unlikely that Leonard had a personal account at Bank Continental or Bank Cantonale.

*** The government did not contend that the $383,000 was income and could not have so contended since there was no proof that the transaction was taxable. In any event, the government specified in the bills of particulars that the omitted income was exclusively Treadwell monies. (A 24a, 36a, 37a)

planations of the Swiss account evidence. It was the government's burden to prove by at the very least, plain, clear and convincing evidence, that Leonard *personally* had a Swiss bank account or had "transactions" with a Swiss bank. The government failed to meet this burden.

> "It may well be that petitioner's answers were not guidelines but were shrewdly calculated to evade. Nevertheless, we are constrained to agree with Judge Lumbard. . . . that any special problems arising from the literally true but unresponsive answer are to be remedied through the 'questioner's acuity' and not by a federal perjury prosecution." *Bronston* v. *U.S., supra,* 409 U.S. at 362.

It cannot be emphasized too strongly that Agent Laski drew the affidavit, not Leonard. Laski was a highly trained Revenue Agent who was a member of the elite group participating in the FBA project. He was a CPA who graduated from law school shortly after interrogating Leonard. If he wanted information about indirect transactions, he should have drafted the affidavit differently. If he wanted information about business (i.e., corporate) accounts Leonard might have, he could have done so more precisely. He could easily have included in the affidavit accounts Leonard controlled or with which he was connected.

Therefore, if the affidavit is ambiguous or imprecise, that fact should not be held against Leonard. It was, after all, a government agent who prepared the affidavit and who determined the scope and content of Leonard's denial.

Eva Brooke's "Swiss bank" evidence is consistent with Leonard's 1971 tax return. She testified that in the summer of 1971 she overheard Leonard offer to deposit money in a Swiss bank account for the benefit, and in the name, of her husband whom Leonard was then seeking to bring into his corporation as a business associate. (A 509-513) During the conversation, which followed drinks, Leonard

said "I have one". (A 511-512) Since this was a social conversation and therefore "loose talk", Leonard could very well have been referring to an account of a corporation in which he had an interest. This testimony was therefore not "clear and convincing" evidence that the foreign bank account provision in Leonard's 1971 tax was false.*

Therefore, since the government never proved the falsity of the Swiss bank affidavit and foreign bank provision, this evidence lacked probative value. It was, however, highly inflammatory and prejudicial. Consequently, the court erred in admitting it.

As a result, defendant suffered substantial injury, since the Swiss bank evidence was well-calculated to lead the jury (which undoubtedly believed that a Swiss bank account is a "hallmark of tax evasion" [A 30]) to conclude that Leonard was guilty of substantial tax evasion and deserved to be punished, irrespective of whether he had in fact committed the particular crime set forth in the indictment.

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* Additionally, Eva Brooke's testimony about what Leonard had said in 1971 was too remote to be probative. Leonard was charged in the indictment with making false statements in his 1967 and 1968 tax returns. Even if Leonard had made a false statement in April 1972 on his 1971 return, this was four years *after* the last tax return year charged in the indictment and therefore hardly relevant to what he may have intended on his 1967 and 1968 returns. Furthermore, Eva Brooke's testimony that Leonard had said he had an account in 1971 had the substantial danger of washing over to and supporting the government's unproven claim that the Swiss bank affidavit (GX 74) given in 1969 was false. The jury likely concluded that Leonard had the same account in 1969 as he did in 1971 when he talked to Mrs. Brooke. However, her testimony was unequivocal that Leonard had said in 1971 only "I have one [i.e. a Swiss account]". (A 511-512)

POINT IV

Leonard was denied a fair trial because: (1) the government obstructed his interviews of prospective witnesses; (2) the Court improperly refused to grant him a continuance to prepare his defense against surprise similar act evidence; and (3) the government's opening contained allegations of criminal conduct that were untrue and never proven.

1. The government improperly obstructed the defendant's interviews of prospective witnesses.

The government repeatedly obstructed defendant's pretrial preparation by insisting on being present during all interviews of prospective government witnesses and instructing them not to answer questions which were clearly relevant to matters covered in Leonard's indictment. (A 79a-251a)

Defendant was denied the opportunity to question Revenue Agent Morris Laski, a key prosecution witness whose credibility was sharply in issue at the trial, either as to his contacts with the prosecutors* or the reasons why Laski had asked Leonard in the course of the audit, whether he had a foreign bank account.**

Perhaps most indicative of the difficulties defendant faced in seeking to obtain information from prospective

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* Q. "Have you discussed the facts with [the prosecutor] on the phone or in person or both?"

Mr. MacDonald: "That's one of the questions he is putting in quotable form and there is no need to answer it?" (A 113a)

** Q. "What was the basis for your inquiry [during the audit] as to whether or not he had a Swiss bank account?'

Mr. MacDonald: "I instruct you not to answer. This is clearly something you want to take up with the Judge in advance of trial, or else you waive your client's rights."

Mr. Tigue: "I have brought it to the Judge's attention. You still persist in intervening in my examination and I maintain the objections I have previously stated and when this transcript is typed up today, I am going to give it to Judge Owen and continue my complaint." (A 123a)

government witnesses is the following portion of the transcript of defense counsel's interview of Special Agent Shulman:

> Q. "Did you ask for any further documentation or papers in connection with the affidavit?
>
> Mr. MacDonald: Until I am advised as to some reason for the admissibility of this whole line, I will stop the whole line.
>
> It seems inconceivable that statement comes in without your client getting on the witness stand and what the agents did to verify or what they negatively did not do is irrelevant until such time as a cross-examinable witness is on the witness stand.
>
> Mr. Tigue: The trial hasn't begun yet and I am conducting my pretrial investigation.
>
> Mr. MacDonald: Educate me.
>
> Mr. Tigue: You are worried about your strategy, whether you should put the statement in in your direct case or rebuttal.
>
> I think this is all improper.
>
> Mr. MacDonald: I solicit some education as to why it is that statement is admissible—
>
> Mr. Tigue: It doesn't have to be admissible when you are interviewing a witness before trial. You know that. We are not in a courtroom.
>
> (Discussion off the record.)
>
> Mr. Tigue: Basically, if I can summarize what we said off the record, it is that I regard the interference by you in the questioning of these various witnesses to be a denial of a fair trial to Mr. Leonard, that is, you are preventing his counsel from determining what the facts are which I regard, even though you don't as important to prepare an adequate defense for him.
>
> I think without that information I may very well be in a position of not being able to defend him, and he may not be in a position to get a fair trial.
>
> That's my basic position.

Mr. MacDonald: Great. *If and when you want to tender his box and stop claiming the Fifth on all of the evidence he possesses, then I will change the rules.* We are operating under rules—

Mr. Tigue: One of the rules we operate under is the Fifth Amendment to the Constitution. He has a right not to talk to you. Prosecutors don't like it. I didn't like it when I was a prosecutor but I lived with it.

Your job is to do justice. My job is to protect my client. I don't have to tell you that. And I don't think it's doing justice when you interpose yourself in an interview when I would like to have privately with this witness and other witnesses because you are applying the Federal Rules of Criminal Procedure or the rules of evidence in a trial, especially in view of the fact that anyone I have ever brought down here, you were permitted to ask any questions you wanted to.

* * *

Q. Basically, Mr. Shulman, you really would like to answer my questions, wouldn't you.

Mr. MacDonald: Don't answer.

Q. What did you do in the investigation from the time you began in March or April of '72 up until June of '72?

I'm sorry, up until—yes—July of '72?

Mr. MacDonald: Same instruction.

Q. After July of '72, what further steps did you take in connection with the investigation?

Mr. MacDonald: Same instruction.

Mr. Tigue: I don't have any further questions in view of your position here, Mr. MacDonald, but I certainly intend to bring it to the Court's attention to get whatever relief I can, either this Court or the Court of Appeals." (A 243a-250a) [Emphasis added]

Defendant duly made a motion to compel the witnesses to answer the challenged questions and to obtain an order preventing the government from continuing to interfere with defendant's pre-trial preparations. The Court denied the motion.* (A 350a)

At the conclusion of the trial, in order to correct, at least in part, an obvious error, the government submitted affidavits from the eight witnesses who the defendant had sought to interview before trial. All eight affidavits were identical in all respects, except the names had been inserted where appropriate.** Each of the affidavits claimed in identical language that the witness desired the assistance of the Assistant U.S. Attorney assigned to the case (rather than an attorney from IRS Regional Counsel) and, further, that the witness would have declined a "private interview" without the prosecutor's presence. (A 29a-33a, 75a-78a)

Irrespective of whether the prosecutor had the right to insist on being present during the interviews, the instructions to the witnesses not to answer the defendant's questions were clearly improper. *U.S.* v. *Matlock,* 491 F.2d 504 (6th Cir. 1974); *U.S.* v. *King,* 368 F. Supp. 130 (M.D.Fla. 1973); *Johnston* v. *N.B.C.,* 356 F. Supp. 904 (S.D.N.Y. 1973); *Coppolino* v. *Helpern,* 266 F. Supp. 930 (S.D.N.Y. 1967); *Gregory* v. *U.S.,* 369 F.2d 185 (D.C. Cir. 1966).

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* The court noted that the defendant had had some interviews with the government's witnesses, which the court asserted was "more than you had any right to expect". (A 350a) The court further held that "absent a showing" that the witnesses wanted to speak to the defendant without the prosecutor being present he would not intervene. However, as the above portions of the transcript demonstrate, it was impossible for the defendant to make such a showing because the prosecutor foreclosed that line of questioning by instructing the witnesses not to answer the questions.

** Identical affidavits were signed by IRS Agents Shulman, Tragna, Singer, Alleva, Levy, Reiner, Sussman and Laski. The venue for the affidavit of Morris Laski was different from the others, since at the time he signed it, he was located in California. (A 29a-33a, 75a-78a)

The court in *Matlock, supra,* held:

> "Witnesses are neither the property of the government nor of the defendant. * * * Instructions to a witness not to cooperate with the other side or to talk to lawyers for the other side would not be proper . . ." *Id.* at 506

The prejudice Leonard suffered was substantial. At the time defendant's counsel interviewed Laski on January 6, 1975 and sought to question him about the Swiss bank account affidavit, the defendant was not aware that this was an FBA project case and further did not know the details of the mail watch as it pertained to Leonard. Indeed, the prosecutor's instructions to the witnesses not to answer questions on this subject blocked, at the very least, discovery of the relevant Post Office regulations and related IRS documents. Thus, the defendant's access to essential information which might have led to possible defenses and witnesses was restricted and his ability fully to prepare a defense improperly hampered.*

2. The Court improperly refused to grant Leonard a continuance to prepare his defense against surprise similar act evidence.

This case presents the precise problem addressed in *U.S.* v. *Baum,* 482 F.2d 1325 (2nd Cir. 1973). In *Baum,* this Court reversed a conviction because the defendant had been denied a continuance to meet surprise similar act proof, where he had, prior to trial, requested information concerning the nature and identity of such evidence.

The first indication Leonard had that the government would seek to prove "similar acts" was on January 2,

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* Moreover, where the prosecutor's conduct violates a defendant's constitutional rights, the defendant need not establish prejudice. See *Gregory* v. *U.S., supra.* In fact, the prosecutor's instructions may have by themselves prevented the defendant from making such a showing.

1975*, four days before the scheduled commencement of the trial.

On January 7, 1975, at a pre-trial hearing, Leonard's counsel advised the trial judge that counsel was in no position to defend Leonard with respect to those similar acts because he had no idea what they were. (A 310a-312a)

Although the court adjourned the trial until January 14, 1975 to allow time for Leonard's attorney to prepare more adequately (Leonard's counsel had been recently substituted), the judge refused to order the government to disclose the similar acts which it intended to prove. Indeed, the judge did not even require the government to advise the court what the alleged similar acts were, but left to the prosecutor's "good judgment"—"having the *Baum* case in mind"—whether disclosure was necessary to avoid prejudicing Leonard's defense (A 444a).

On Friday afternoon, January 10, 1975, the government (which had this information from at least early December 1974) delivered to Leonard's counsel's office copies of $383,000 in official Chase Manhattan Bank checks payable to Leonard's order which the government intended to prove came from a Swiss bank account. (A 72a) The apparent purpose of this evidence was to show circumstantially the falsity of the affidavit which Leonard had signed in 1969 denying he had a Swiss account. Since trial was scheduled for the following Monday, the delivery at this late hour was useless since it prevented the defendant from doing anything to meet this proof.

On the following Monday, January 13, 1975, the day trial was to begin, the defendant notified the court that these checks came as a total surprise to him, that he was "in no position to defend that charge", and that he needed a continuance to meet this proof. Nevetheless, the court declined to grant the continuance. (A 10-11)

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* On that date, Leonard's attorney received a copy of the government's requests to charge, which included a request for an instruction on similar acts. (A 310a)

During the trial, when the government called Harris Egan of Chase Manhattan to establish that the $383,000 in checks had been received from a Swiss bank, Leonard once again moved for a continuance. (A 503) Once more the court refused the request.* Similarly, the defense did not learn that Eva Brooke would testify until just before she took the stand.

There was no proper reason for nondisclosure of the identity of these witnesses and evidence. Neither would have been placed in jeopardy by disclosure. While this testimony may have been important to the government, it was crucial to the defendant to meet critical and damaging proof of a crime neither charged in the indictment nor specified in the government's bills of particulars.

As this court held in *U.S. v. Baum, supra:*

> ". . . the defendant had little or no opportunity to meet the impact of this attack in the midst of the trial. This precarious predicament was precipitated by the prosecutor . . .
>
> Ordinarily it is disclosure, rather than suppression, that promotes the proper administration of criminal justice . . .
>
> It is the duty of the government to present its case against the defendant fairly. Little can be added to Justice Traynor's statement—'A defendant has hardly had a fair trial if he has been denied the opportunity

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* The government, by delaying notifying defendant until the last moment that it would seek to prove similar acts placed the court in the untenable position of choosing between delaying a one-week jury trial for possibly seven days to enable defense counsel to travel to Switzerland to meet unexpected evidence or depriving the defendant of an adequate opportunity to rebut this proof. What made defense counsel's job even more difficult here (but all the more important) was the fact that Mr. Egan testified about documents which had been destroyed two years before and were theretofore not available at trial. Furthermore, the underlying transactions themselves had occurred in 1968, that is, seven years before, hardly the recent past, and therefore exceedingly difficult to investigate on short notice.

> to discover evidence or information crucial to his defense . . .
>
> The failure to reveal [the similar-act witness's] identity until he was presented as a witness, confronted the trial judge with the hard choice of interruption of the trial or denial to the defense of a reasonable opportunity of meeting the severe impact of this aspect of the prosecutor's evidence. Such tactics were condemned, and called for the reversal in *United States* v. *Kelly*, 420 F.2d 26, 29 (2nd Cir. 1969). In the language of Judge Smith: 'The course of the government smacks too much of a trial by ambush, in violation of the spirit of the rules'." *Id.* at 1331-1332.

Additionally, the government further ambushed the defendant by concealing the fact that Eva Brooke would be called as a witness. Prior to her appearance, the government made an *ex parte* application to the trial court for an order requesting judicial assistance in England (where Mrs. Brooke lived) to compel her presence in New York.* Despite the fact that the defendant had, prior to trial, requested disclosure of the identity of similar-act witnesses, discussions between the prosecutor and the trial court on this application were conducted outside the defendant's presence. (A 238-239)

There was no legitimate reason for the government to do this; there was no danger to the witness or any other proper purpose for concealment. There was further no sound judicial reason for this *ex parte* procedure. The result was that the trial court, doubtlessly unwittingly, facilitated the withholding of the identity of a similar act witness. Realistically, the only purpose for the government's withholding this information was to "ambush" the defendant by concluding its case in a dramatic fashion.

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* See "Letters Rogatory to the Appropriate Judicial Authority" in London, England to compel Eva Brooke to testify at the trial. (A 448a-451a)

3. The government's opening contained allegations of criminal conduct that were untrue and never proven.

The government, in its opening statement, charged that Leonard had committed other crimes and had made other false statements to the IRS during the course of the audit. These allegations were highly inflammatory because they were both untrue and never proven.

A. The prosecutor strongly implied to the jury that Leonard received "kickbacks" from Treadwell. (A 29) As the government well knew, it would never offer any evidence of commerical bribes because the UCC contract specifically provided that Leonard would receive a stated percentage of the monies paid to Treadwell for supervisory services on the Taft project. The payments were pursuant to contract, and not "kickbacks", either legal or illegal.* (GX 3, ¶ 3(e))

B. The prosecutor charged that Leonard falsely stated to IRS Special Agent Norman Levy and IRS Auditor Joseph Tragna that the delay in depositing four 1967 UCC checks until 1968 was due to "litigation" with UCC. (A 26-27) Neither Levy nor Tragna were called as government witnesses, and therefore there was no evidence that the conversation had even occurred. Since the agents were clearly available, the only reason they were not called was tactical.** But the prosecutor, nonetheless, offered testimony as to the absence of litigation, (A 93) without connecting it up to anything Leonard may have told the

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* The government's opening statement filled ten pages of the transcript, half of which was devoted to allegedly false statements and other misconduct which the government never proved. (A 20-30)

** This is not a situation, as in *U.S.* v. *West*, 486 F.2d 468 (6th Cir. 1973), where the government's opening was based on a statement from a witness who ultimately turned hostile and refused to testify in a manner consistent with the statement or who, when subpoenaed, asserted his Fifth Amendment privilege and declined to testify altogether. Here, Levy and Tragna were government agents who were clearly available but nevertheless were not called to testify.

IRS, (See A 368) and then referred to the absence of "litigation" in his summation as though he had proved his point. (A 931)

C. The prosecutor claimed that Leonard failed to supply documentation requested by the IRS regarding the payment delay and certain cross-outs in the UCC contract. (A 28) However, Levy and Tragna did not testify, and Laski admitted that he never asked Leonard to produce any documents concerning the contract changes. (A 295, 303-304)

D. The prosecutor claimed that Leonard "had a Swiss bank account from which he received hundreds of thousands of dollars during the course of 1968 *and other years*". [Emphasis added] (A 30) Even assuming that the checks from Chase were admissible and tended to show Leonard received monies from a Swiss bank account in 1968, there was no evidence whatsoever that Leonard received any monies from Switzerland in any other year.

These unproved allegations of other crimes and misconduct, which related to false statements to the IRS—the very charges in the indictment—undoubtedly prejudiced the jury against Leonard. They were designed and had the effect of convincing the jury that Leonard was guilty of a continuous and gross pattern of tax evasion and purposeful concealment. Cf. *Leonard* v. *U.S.*, 277 F.2d 834 (9th Cir. 1960)* and *U.S.* v. *Signer*, 482 F.2d 394 (6th Cir. 1973).

POINT V

The government failed to prove that Leonard omitted income in his 1967 tax return.

The indictment charged in Count I that Leonard omitted from his adjusted gross income for 1967 $24,168 which he received from Treadwell in connection with the UCC contract.

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* The defendant in that case has no relation to the defendant in this case.

The only witness the government called to testify as to the preparation of the 1967 return was Marion Bardes, a bookkeeper who did free-lance work for Leskowicz, Brower & Driver and who did some bookkeeping for Leonard Corp. in 1968. (A 446)

Miss Bardes testified that she prepared a penciled copy of the top document in GX 92, (the accounting firm's tax file for Leonard) which was merely the first page of a draft of Leonard's 1967 Federal return. (A 431) She did *not* prepare the final return (which, as we explain below, was substantially different from her draft):

> "Q. Were you the person who prepared the 1967 income tax returns for Mr. Leonard?
>
> A. Personal return?
>
> Q. Yes, Ma'am.
>
> A. *No, sir.*
>
> Q. Do you know if it was someone in the firm of Leskowicz, Brower and Driver?
>
> A. I would assume so, yes.
>
> Q. But you really don't have your own personal knowledge?
>
> A. No." (A 430-431). (Emphasis added)

Moreover, she could not even recall where she obtained the figures for the one page she did prepare:

> "Q. Could you tell us where you got the information to put the numbers on that [penciled] return?
>
> A. Honestly, I can't tell you. I would assume that I got them through Mr. Leskowicz." (A 432)

Most important of all, however, is the fact that Miss Bardes' draft differed materially from the Schedule C (Profit or Loss from Business) actually filed by Leonard as a part of the 1967 return. (GX 1)

The draft indicated that net Schedule C income totalled $258,564, while the actual return showed $241,707, a difference of approximately $17,000 (not very much different from the amount the indictment charged as omitted). Why

were these figures different? Who changed them? What were the circumstances? What was Leonard's connection, if any, with the changes?* There was simply no testimony or evidence adduced by the government which reconciled these conflicts or provided answers to these questions.

A further significant deficiency in the government's proof is the failure to show specifically what income was included (or excluded) in Schedule C gross receipts. The tax return merely states the total amount, $461,000, but does not give any break-down of the items that comprised this figure.

Miss Bardes testified that she analyzed Leonard's monthly statements from First National City Bank. (GX 76) (A 444) This analysis (GX 77) shows gross deposits of $729,399.13, $291,000 of which she attributed to UCC. There was no testimony as to the further make-up of the $461,000 in gross receipts.

The only documents which are conceivably relevant to the question are GX 92, pages 01904 and 01905.** The record is unclear whether Miss Bardes prepared both pages or only 01904.

Document 01904 contains a heading, "Schedule C JD Leonard 1967", and under "Receipts" there is a list of seven companies and figures totalling $553,423.13. Document 01905 is headed "J.D. & S.S. Leonard 1967" and lists, under the heading "Income", four companies and fig-

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* There were still other differences between the draft and the final. A few examples follow:

Item	*Draft* (*GX 92*)	*Final* (*GX 1*)
Line 9 (Total income)	$246,429.90	$259,051.97
Line 11a (Total itemized deductions)	96,758.00	98,143.10
Line 11d (Adjusted gross income)	157,871.90	159,108.87
Line 12 (Tax)	82,175.45	82,056.40

** GX 92 is, as previously indicated, Leskowicz's file for Leonard. The government numbered each document separately when it obtained the file.

ures totalling $461,000. Some of the names listed on 01905 are different from those on 01904, and some of the numbers listed alongside the named companies are also different.*

At the conclusion of the government's case, the defendant moved to dismiss Count I on the ground that the government had failed to connect the 1967 return and the omitted income. (A 580) The court, however, erroneously denied defendant's motion. (A 584)

It is clear that the government failed to prove that Leonard omitted certain Treadwell payments from his 1967 tax return. There was no testimony as to what income was actually included in that return, and the documents are silent on that question. The jury, therefore, had no reasonable basis for concluding that Leonard failed to report specific items of income on his 1967 return.

Indeed, when the government called Leskowicz to testify in rebuttal, it carefully avoided asking him the standard questions relating to the preparation of the return and Leonard's alleged concealment of Treadwell income and, specifically, whether the Treadwell payments were in fact omitted in the final 1967 return. (GX 1)

Therefore, Leonard's conviction of Count I of the indictment should be reversed.

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* More particularly, the following appears on the two documents:

01904 *"Receipts"*		*01905* *"Income"*	
UCB Catalyst	$ 59,718.25	Nisson (sic)	$100,000.00
UCC	291,000.00	Japan Gas Chemical Co.	20,000.00
GAF Catalyst	17,479.88	Union Carbon & Carbide	291,000.00
ICI Catalyst	27,225.00	British Hydrocarbon Chem.	50,000.00
Japan Gas	18,000.00		
Nisson	90,000.00		
BHC	50,000.00		
	$553,423.13		$461,000.00

POINT VI

The Court erred in refusing to charge the jury on the consequences of the assignment to Leonard Corp. of the UCC contract and in refusing to admit Leonard Corp.'s tax return as proof of its earnings.

The government proved as part of its direct case that effective February 1, 1968, Leonard, with UCC's consent, had assigned to Leonard Corp., his Subchapter S (tax-option) corporation, all of Leonard Process' rights under the UCC contract, and Leonard Corp. had simultaneously assumed all of Leonard Process' obligations thereunder. (A 98-99) (GX 65)

Although Count II of the indictment charged, and the government proved, that Leonard did not include in his 1968 federal income tax return income totalling $58,684.42 (which monies the government's bills of particulars identified as being the proceeds of eleven checks received from Treadwell in 1968 in connection with the UCC contract*), Leonard nevertheless did not thereby violate § 7206(1) of the Internal Revenue Code because he had no duty to report the receipt of $52,455.22 of these monies, since that sum represented post-January 31, 1968 payments that were the property of Leonard Corp., and not Leonard personally.

Were it not for the fact that Leonard diverted the aforesaid Treadwell payments, there could be no question that they should have been included in Leonard Corp.'s, rather than Leonard's 1968 return. Leonard's first obligation to report these payments would not have arisen until the monies were either distributed to him in the form of dividends paid out of the corporation's earnings or profits, or until he filed his 1969 tax return** following the end of Leonard Corp.'s initial fiscal year.

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* These consisted of one check for $6,229.20 (dated January 10, 1968) and ten other checks (dated February 20th through November 6, 1968) totalling $52,455.22 (GX 53-63).

** Section 1373 of the Internal Revenue Code provides that a shareholder of a Subchapter S corporation must include in his

(*footnote continued on following page*)

The Diversion of Funds

The government sought to prove, however, that Leonard had embezzled $52,455.22 of Leonard Corp.'s assets during calendar 1968 by personally cashing the Treadwell checks and keeping the proceeds. (GX 53-63) These sums, the government contended and the district court agreed, were includible in Leonard's gross income under the principles of *James* v. *U.S.*, 366 U.S. 213 (1961).

In so doing, however, the government and the court completely overlooked *Dizenzo* v. *C.I.R.*, 348 F.2d 122 (2nd Cir. 1965), where this Court held that when a controlling shareholder misappropriates his corporation's income, he should be treated as though he received a constructive dividend in the amount of the diverted funds, and taxed on it *to the extent* of the corporation's earnings and profits, with the balance, if any, regarded as a return of capital. See also *Simon* v. *C.I.R.*, 248 F.2d 869 (8th Cir. 1957) and Gardner, *The Tax Consequences of Shareholder Diversions in Close Corporations*, 21 Tax L. Rev. 223 (1966).

Leonard Corp. had a Net Operating Loss of $73,742.33 in fiscal 1968/69

Wendy Brewer, an IRS employee, testified that she was unable to locate any federal income tax return (Form 1120S) filed by Leonard Corp. for its fiscal year ending January 31, 1969. (A 78) However, the proof shows that Leskowicz, Brower & Driver initially prepared a return that reflected a net operating loss of $29,017.77 (GX 94) (A 474-475) and thereafter superseded it with an amended return which indicated that Leonard Corp.'s net operating *loss* for fiscal 1968 was actually $73,742.33 (DX X) (A 475) The amended return was signed by both Jackson D. Leonard and his accountants, Leskowicz, Brower & Driver

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(*footnote continued from preceding page*)

gross income, *for the year in which the corporation's taxable year ends*, his pro rata share of the corporation's undistributed taxable income for the corporation's taxable year. Leonard Corp.'s initial fiscal year ended January 31, 1969.

but Leskowicz neglected to file it and it was found in Leskowicz's files which were produced at trial.*

The books and records of Leonard Corp., (GX 87) maintained by the certified public accounting firm of Leskowicz, Brower & Driver, demonstrate that Leonard Corp. sustained a loss in fiscal 1968/69 of $73,742.33.

Although the amended return was identified by a government witness (Emil A. Nothofer) as a return prepared in the regular course of business by the Leskowicz firm (A 466), the court improperly limited the admission of the return solely for the purpose of showing that Leonard Corp.'s accountants had prepared a tax return for the period ending January 31, 1969, but not as proof of Leonard Corp.'s earnings or losses for fiscal 1968/69. (A 472-473)

While defendant concedes that Leonard Corp.'s amended 1120S does not include the $52,455.22 of Treadwell income Leonard diverted, even if that sum is added to Leonard Corp.'s operations for fiscal 1968 the corporation would still have an net operating loss of $21,287.11 for that year.

Consequently, under the rule of *Dizenzo, supra,* the misappropriated sums were not taxable to Leonard in 1968. Therefore, Leonard did not violate § 7206(1) when he failed to include the $52,455.22 in his 1968 adjusted gross income.

Burden of Proof

The government has the burden of proving every element of the crime beyond a reasonable doubt. *McCormick on Evidence* (1954) § 321. If one of the issues is whether income was reported, the government must prove that the taxpayer was required to include the income in his return.

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* The relevant page from Leonard Corp.'s general ledger (GX 87) is consistent with and supports the amended fiscal 1968 1120S return of the corporation.

Once the UCC contract (which included the right to receive the Treadwell payments) was proved to have been assigned to Leonard Corp. (A 98-99), it was incumbent upon the government to prove that Leonard nevertheless had to include these payments in his 1968 income.

Since the only theory under which the payments were taxable to Leonard is if they were constructive dividends, it was the government's duty to prove that Leonard Corp. had earnings and profits. Cf. *Dizenzo* v. *C.I.R., supra.* This, the government wholly failed to do.

Materiality

The indictment charged that Leonard had subscribed income tax returns which he did not believe to be correct as to "material" matters. Leonard's reported adjusted gross income for 1968 was $134,276.00 before deductions. Since the $52,455.22 in Treadwell payments had been assigned to Leonard Corp. and therefore did not have to be included in Leonard's personal return for 1968, the only additional income which the government proved should have been reported by Leonard in 1968 was a single check for $6,229.20.

Since $6,229.20 is less than 5% of Leonard's reported 1968 adjusted gross income, a properly instructed jury may well have concluded that this omission was not material.

The defendant requested the court to charge the jury on the constructive dividend theory and also on the question of materiality.* However, as noted, the court declined to do so. (A 838)

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* The defendant's "Request to Charge E" was as follows:

"It is impossible from a legal point of view for the sole shareholder of a corporation to embezzle funds from his corporation. Money received by Mr. Leonard from his corporation, The Leonard Process Co., Inc., is income to Mr. Leonard only to the extent that there are current or accumulated earnings and

(*footnote continued on following page*)

The refusal of the trial court to instruct the jury as requested meant that the jury considered Count II on an erroneous legal theory.

Consequently, Leonard's conviction on Count II of the indictment should be reversed, and Leonard should be granted a new trial on that charge.

Since the jury's verdict with respect to Count I may well have been influenced by its verdict on Count II, the entire conviction should be reversed and a new trial ordered.

POINT VII

The court erred when it failed to dismiss the indictment which was founded on materially false grand jury testimony.

The original indictment returned by the grand jury charged the defendant with two counts of subscribing tax returns which omitted material amounts. The indictment also contained a third count which charged Leonard with submitting to the IRS in May 1970 a false document in violation of 18 U.S.C. Section 1001. The allegedly false document was a copy of the UCC contract (GX 66) which contained two lines of cross-outs over the portion which provided that Leonard was to receive a 10% override on

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(*footnote continued from preceding page*)

profits. The proof in this case shows that in the first year of operation, the corporation sustained a loss of approximately $73,000. Therefore, I instruct you as a matter of law that the checks addressed to The Leonard Process Co., Inc. from the period February 1968 through November 1968 are returns of capital and are not taxable. The government has the obligation of proving each element charged in the indictment. The government must prove that the checks received in 1968 were income to Jackson D. Leonard. If you find that the government has failed to prove the existence of current or accumulated earnings and has failed to establish the basis of Mr. Leonard's stock, then you must acquit the defendant on Count Two of the indictment."

the engineering work for the Taft and South Charleston plants.*

Prior to trial, the government moved to dismiss the third count on the ground that it was barred by the statute of limitations. The government informed defense counsel "on the record" on or about December 24, 1974 that although Count Three charged that the contract had been submitted to the IRS in May *1970,* and was therefore within the period of the Statute of Limitations, the grand jury testimony on this subject had been erroneous in that the contract was actually exhibited to the Agent in May or June *1969.* (A 71a)

As a result of this information, the defendant moved, on December 31, 1974, pursuant to *United States* v. *Basurto,* 497 F.2d 781 (9th Cir. 1974), for an order dismissing the entire indictment on the ground that it had been based on false or inaccurate grand jury testimony. (A 70a) The trial court denied the motion but sealed the grand jury minutes for inspection by this Court.

If, as the government stated, the UCC contract had been shown to Agent Laski in May or June of 1969 (rather than in 1970) this meant that the grand jury had been misinformed as to a highly material fact.

It must be assumed (since the defendant has not seen these minutes) that the government's position before the grand jury was that Leonard had purposely omitted the Treadwell payments in 1967 and 1968 and that *subsequently,* when questioned about them, Leonard produced an altered UCC contract that concealed their existence.

The actual facts were quite to the contrary. According to the government, the UCC contract was displayed to

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* As previously noted, Leonard's compensation under the UCC contract consisted of essentially two types of payments: a fixed fee of $750,000, and a 10% override fee for supervising certain detailed engineering work to be performed by Treadwell. Since UCC decided not to build the South Charleston plant, Treadwell did no engineering work there and Leonard, of course, received no supervisory fee for that plant. This was apparently the reason why the provision in the UCC contract had been crossed out.

Agent Laski in May or June 1969.* *Thereafter* Leonard caused his 1968 return to be filed.** Obviously, Leonard (who had been audited nearly every year for the past twenty years and who had had various disputes with the IRS which had culminated in his filing a petiiton in Tax Court for review of IRS determinations for four previous years (A 71a)) would not in August 1969 purposely omit Treadwell payments on his 1968 return when he had been told that the IRS was investigating such payments for 1967.

Laski testified at trial that when he saw Leonard and Leskowicz on March 17 or 18, 1969, he questioned Leonard about the crossed-out portion of the UCC contract.

> "I asked him about Section 3(e), about the override, where there was a crossing out but no initials, and he said the contract was changed [referring to other changes] once again." (A 207)***

Leonard's statement was absolutely accurate. The contract was changed in that regard since UCC had decided not to go forward with the South Charleston plant and therefore Leonard was not entitled to a 10% override from Treadwell for supervising that engineering work, since there was none. It must be assumed that the grand jury was not informed of this fact either and more importantly that there was an entirely legitimate and plausible reason for the cross-outs.

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* Even the revised government position is inconsistent with Laski's trial testimony. Laski testified, and DX G, his activity report indicated, that the only dates in 1969 on which Laski met with Leonard or Leskowicz (Leonard's accountant) were January 8, 9 and 10, February 4 and March 17 and 18. Moreover, Laski stated at trial that he questioned Leonard about the cross-outs in March, 1969. (A 309-310)

** Leonard's 1968 return, pursuant to an extension granted by the IRS, was filed on or about August 15, 1969.

*** Additionally, it must be assumed that the grand jury was also not told of the tax consequences of the assignment of the UCC contract to Leonard's Subchapter S corporation, Leonard Corp., and that the vast majority of the Treadwell payments in 1968 were not reportable on Leonard's 1968 return.

In *Basurto, supra,* the government, prior to trial, informed defense counsel, rather than the court, that there had been false grand jury testimony about material facts involved in the case. In reversing the conviction, the court applied the test of what the grand jury "might" have done had it been accurately informed as to the facts. *Id.* at 785.

While the challenged testimony in *Basurto* was purposely false—i.e., perjured testimony—the effect on the grand jury is the same regardless of whether the false testimony was intentionally false or not. The grand jury returned an indictment in this case that was clearly based, at least in part, on materially false or inaccurate testimony.

This false testimony "has poisoned the water in this reservoir, and the reservoir cannot be cleansed without first draining it of all impurity." *Basurto, supra,* at 786, citing *Mesarosh* v. *U.S.*, 352 U.S. 1, 14 (1956).

Therefore, the conviction should be reversed and the indictment dismissed.

CONCLUSION

The judgment of conviction should be reversed and the indictment dismissed.

Alternatively, a new trial should be granted and all evidence obtained as a result of the illegal mail watch and the failure of the IRS to properly warn Leonard of his constitutional rights should be suppressed.

Respectfully submitted,

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ADDENDUM

"26 U.S.C. § 7206. Fraud and false statements

Any person who—

(1) Declaration under penalties of perjury.—Willfully makes and subscribes any return, statement, or other document, which contains or is verified by a written declaration that it is made under the penalties of perjury, and which he does not believe to be true and correct as to every material matter; or

(2) Aid or assistance.—Willfully aids or assists in, or procures, counsels, or advises the preparation or presentation under, or in connection with any matter arising under, the internal revenue laws, of a return, affidavit, claim, or other document, which is fraudulent or is false as to any material matter, whether or not such falsity or fraud is with the knowledge or consent of the person authorized or required to present such return, affidavit, claim, or document . . . shall be guilty of a felony."

"26 U.S.C. § 6064. Signature presumed authentic

The fact that an individual's name is signed to a return, statement, or other document shall be prima facie evidence for all purposes that the return, statement, or other document was actually signed by him."

"18 U.S.C. § ~~1072~~ 1702. Obstruction of correspondence

Whoever takes any letter, postal card, or package . . . which has been in any post office or authorized depository, or in the custody of any letter or mail carrier, before it has been delivered to the person to whom it was directed, with design to obstruct the correspondence, or to pry into the business or secrets of another, . . . shall be fined not more than $2,000 or imprisoned not more than five years, or both."

CHIEF POSTAL INSPECTOR
Washington, DC 20260

May 5, 1975

Mr. Alan Kanzer, Esq.
Walter, Conston, Schurtman
and Gumpel, P. C.
Attorneys at Law
330 Madison Avenue
New York, New York 10017

Dear Mr. Kanzer:

Your letter of April 18, 1975, to the U. S. Postal Service, Attention: General Counsel, has been referred to me for reply. In your letter you requested, pursuant to the Freedom of Information Act, copies of Postal Service regulations, postal bulletins, and any other material relevant, during 1968 and 1969, to the initiation of a mail cover at the request of another agency.

On June 17, 1965, the Post Office Department published new regulations governing the use of mail covers in Postal Bulletin No. 20478, a copy of which is enclosed. These regulations are still in effect today. These regulations were subsequently published in Part 861 of the Postal Manual of the old Post Office Department, supplemented by section 233.2 of the Postal Service Manual. Enclosed are copies of these regulations. Also enclosed is a copy of the mail cover regulations which were recently republished in the Federal Register. This republication makes no substantive changes in mail cover procedures or safeguards, but it updates the provisions dealing with the delegation of mail cover authority to reflect the present organizational structure of the Postal Inspection Service.

Sincerely,

William J. Cotter
Chief Inspector

Enclosures

Subchapter 869 MAIL COVERS

Part 861

ADMINISTRATION

861.1 POLICY

The Post Office Department has established rigid controls and supervision with respect to the use of mail covers as investigative or law enforcement techniques.

861.2 SCOPE

These regulations establish the sole authority and procedure for initiating processing, placing and using mail covers. Any other regulations inconsistent or in conflict with these regulations are of no effect for postal employees.

861.3 DEFINITIONS

For purposes of these regulations, the following terms are hereby defined:

a. "Mail cover" is the process by which a record is made of any data appearing on the outside cover of any class of mail matter, including checking the contents of any second-, third- or fourth-class mail matter as now sanctioned by law, in order to obtain information in the interest of (1) protecting the national security, (2) locating a fugitive, or (3) obtaining evidence of commission or attempted commission of a crime.

b. "Fugitive" is any person who has fled from the United States or any State, territory, the District of Columbia or possession of the United States, to avoid prosecution for a crime, to avoid punishment for a crime or to avoid giving testimony in a criminal proceeding.

c. "Crime," for purposes of these regulations, is any commission of an act or the attempted commission of an act that is punishable by law by imprisonment for a term exceeding 1 year.

d. "Law enforcement agency" is any authority of the Federal Government or any authority of a State or local government one of whose functions is to investigate the commission or attempted commission of acts constituting a crime.

861.4 AUTHORIZATIONS--CHIEF POSTAL INSPECTOR

.41 The Chief Postal Inspector is the principal officer of the Post Office Department in the administration of all matters governing mail covers. He may delegate by written order any or all authority in this regard to not more than four subordinate officials within his Bureau.

.42 The Chief Postal Inspector, or his designee, may order mail covers under the following circumstances:

a. When he has reason to believe the subject or subjects of the mail cover are engaged in any activity violative of any postal statute.

b. When written request is received from any law enforcement agency wherein the requesting authority stipulates and specifies the reasonable grounds that exist which demonstrate the mail cover is necessary to (1) protect the national security, (2) locate a fugitive, or (3) obtain information regarding the commission or attempted commission of a crime.

c. Where time is of the essence, the Chief Postal Inspector, or his designee, may act upon an oral request to be confirmed by the requesting authority in writing within 2 business days. However, no information shall be released until an appropriate written request is received.

861.5 POSTAL INSPECTORS IN CHARGE

.51 All Postal Inspectors in Charge, and not more than three designees pursuant to delegations in writing, may order mail covers under the following circumstances:

a. Where he has reason to believe the subject or subjects are engaged in an activity violative of any postal statute.

b. Where written request is received from any law enforcement agency of the Federal, State, or local governments, wherein the requesting authority stipulates and specifies the reasonable grounds that exist which demonstrate the mail cover would aid in the location of a fugitive, or that it would assist in obtaining information concerning the commission or attempted commission of a crime. Excepting fugitive cases, any request from a Federal agency for a mail cover and the determination made shall promptly be transmitted to the Chief Postal Inspector for review.

.52 Except where mail covers are ordered by the Chief Postal Inspector, or his designee, request for mail covers must be approved by the Postal Inspector in Charge, or his designee, in each district in which the mail cover is to operate.

.53 Where time is of the essence, the Postal Inspector in Charge, or his designee, may act upon an oral request to be confirmed by the requesting authority in writing within 2 business days. However, no information shall be released until an appropriate written order is received.

861.6 LIMITATIONS

.61 No persons in the postal service, except those employed for that purpose in dead-mail offices, may break or permit breaking of the seal of any matter mailed as first-class mail without a search warrant, even though it may contain criminal or otherwise unmailable matter, or furnish evidence of the commission of a crime.

.62 No mail covers shall include matter mailed between the mail cover subject and his known attorney-at-law.

.63 No officer or employee of the postal service other than the Chief Postal Inspector, or Postal Inspectors in Charge, and their designees, are authorized to order mail covers.

.64 Excepting mail covers ordered upon subjects engaged, or suspected to be engaged, in any activity against the national security, or activity violative of any postal law, no mail cover order shall remain in force and effect for more than 30 days. At the expiration of such period, or prior thereto, the requesting authority may be granted additional 30-day periods under the same conditions and procedures applicable to the original request.

.65 No mail cover shall remain in force longer than 120 days unless personally approved for further extension by the Chief Postal Inspector.

.66 Excepting fugitive cases, no mail cover shall remain in force when the subject has been indicted for any cause. If the subject is under investigation for further criminal violations, a new mail cover order must be requested consistent with these regulations.

861.7 RECORDS

.71 All requests for mail covers, with records of action ordered thereon, and all reports issued pursuant thereto, shall be deemed within the custody of the Chief Postal Inspector. However, the physical housing of this data shall be at the discretion of the Chief Postal Inspector.

.72 The Postal Inspectors in Charge shall submit copies of all requests for mail covers to the Chief Postal Inspector, together with reports of the action ordered thereon.

.73 If the Chief Postal Inspector determines a mail cover was improperly ordered by a Postal Inspector in Charge or his designee all data acquired while the cover was in force shall be destroyed, and the requesting authority notified of the discontinuance of the mail cover and the reasons therefor.

.74 Any data concerning mail covers shall be made available to any mail cover subject in any legal proceeding through appropriate discovery procedures.

.75 The retention period for files and records pertaining to mail covers shall be 8 years.

861.8 REPORTING TO REQUESTING AUTHORITY

Once a mail cover has been duly ordered, authorization may be delegated to any officer in the postal service to transmit mail cover reports directly to the requesting authority. Where at all possible, the transmitting officer should be a Postal Inspector.

861.9 REVIEW

.91 The Chief Postal Inspector, or his designee, shall review all actions taken by Postal Inspectors in Charge or their designees upon initial submission of a report on a request for mail cover.

.92 The Chief Postal Inspector's determination in all matters concerning mail covers shall be final and conclusive and not subject to further administrative review.

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POSTAL BULLETIN

Instructions and Information for Postal Employees
Published Weekly

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All Postal Installations

5-Cent Dante Alighieri Commemorative Postage Stamp

The 5-cent stamp commemorating the 700th anniversary of the birth of the great Italian poet, Dante Alighieri, will be initially released through the San Francisco, Calif., post office, on July 17, 1965.

POSTMASTERS SHALL NOT PLACE THIS STAMP ON SALE BEFORE JULY 18, 1965

Size: 0.81" x 1.44" (vertical)
ISSUED IN PANES OF 50
Color: Maroon on tan paper
Initial printing: 112 million

Douglas Gorsline's design simulates the style of early Florentine allegorical paintings. Dante is shown wearing a laurel wreath, symbolic of poetry, against a background related to the poem "The Divine Comedy."

113 891*—65

To obtain first-day cancellations, collectors may submit requests to the Postmaster, San Francisco, Calif. 94101. See Postal Manual, section 145.3. Selected mint stamps will be available at the Philatelic Sales Agency, Post Office Department, Washington, D.C. 20260, on and after July 19, 1965.

All classes of post offices will receive an initial supply of the stamps under the automatic distribution schedule.

First- and second-class post offices requiring additional *bulk quantities* may submit a separate requisition (Form 3356) to the Bureau of Engraving and Printing (Item 456) with memorandum, POD 31, stating that the stamps are required in addition to those automatically furnished.

All post offices requiring *less than bulk* quantities in addition to the automatic distribution may submit a separate requisition (Form 17) to their RDPO and endorse at top "Additional." All requisitions not so endorsed will be returned.—*Office of the Special Assistant to the Postmaster General, 6-17-65.*

All Postal Personnel

MAIL COVERS

Effective immediately, the following regulations govern procedures concerning mail covers.

Policy:

It is hereby declared to be the policy of the Post Office Department that rigid controls and supervision be established with respect to the use of mail covers as investigative or law enforcement techniques. In order that this policy be effectively promulgated, implemented and enforced, the following regulations are adopted.

Scope:

The following regulations hereby establish the sole authority and procedure for the initiating, processing, placing and using of mail covers. Any other regulations inconsistent or in conflict with these regulations are of no effect for postal employees.

Definitions:

For purposes of these regulations, the following terms are hereby defined:

"Mail cover" is the process by which a record is made of any data appearing on the outside cover of any class of mail matter, including checking the contents of any second, third or fourth class mail matter as now sanctioned by law, in order to obtain information in the interest of (a) protecting the national security, (b) locating a fugitive, or (c) obtaining evidence of commission or attempted commission of a crime.

"Fugitive" is any person who has fled from the United States or any State, territory, the District of Columbia or possession of the United States, to avoid prosecution for a crime, to avoid punishment for a crime or to avoid giving testimony in a criminal proceeding.

"Crime," for purposes of these regulations, is any commission of an act or the attempted commission of an act that is punishable by law by imprisonment for a term exceeding one year.

"Law enforcement agency" is any authority of the Federal Government or any authority of a State or local government one of whose functions is to investigate the commission or attempted commission of acts constituting a crime.

Authorizations—Chief Postal Inspector:

The Chief Postal Inspector is the principal officer of the Post Office Department in the administration of matters governing mail covers. And

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MAIL COVERS

(Continued from p. 1)

he may delegate by written order any or all authority in this regard to not more than four subordinate officials within his Bureau.

The Chief Postal Inspector, or his designee, may order mail covers under the following circumstances:

1. Where he has reason to believe the subject or subjects of the mail cover are engaged in any activity violative of any postal statute.

2. Where written request is received from any law enforcement agency wherein the requesting authority stipulates and specifies the reasonable grounds that exist which demonstrate the mail cover is necessary to (a) protect the national security, (b) locate a fugitive, or (c) obtain information regarding the commission or attempted commission of a crime.

3. Where time is of the essence, the Chief Postal Inspector, or his designee, may act upon an oral request to be confirmed by the requesting authority in writing within two business days. However, no information shall be released until an appropriate written request is received.

Postal Inspectors in Charge:

All Postal Inspectors in Charge, and not more than three designees pursuant to delegations in writing, may order mail covers under the following circumstances:

1. Where he has reason to believe the subject or subjects are engaged in an activity violative of any postal statute.

2. Where written request is received from any law enforcement agency of the Federal, State, or local governments, wherein the requesting authority stipulates and specifies the reasonable grounds that exist which demonstrate the mail cover would aid in the location of a fugitive, or that it would assist in obtaining information concerning the commission or attempted commission of a crime. Excepting fugitive cases, any request from a Federal agency for a mail cover and the determination made shall promptly be transmitted to the Chief Postal Inspector for review.

3. Except where mail covers are ordered by the Chief Postal Inspector, or his designee, request for mail covers must be approved by the Postal Inspector in Charge, or his designee, in each district in which the mail cover is to operate.

4. Where time is of the essence, the Postal Inspector in Charge, or his designee, may act upon an oral request to be confirmed by the requesting authority in writing within two business days. However, no information shall be released until an appropriate written order is received.

Limitations:

1. No persons in the Postal Service, except those employed for that purpose in dead-mail offices, may break or permit breaking of the seal of any matter mailed as first-class mail without a search warrant, even though it may contain criminal or otherwise unmailable matter, or furnish evidence of the commission of a crime.

2. No mail covers shall include matter mailed between the mail cover subject and his known attorney-at-law.

3. No officer or employee of the Postal Service other than the Chief Postal Inspector, or Postal Inspectors in Charge, and their designees, are authorized to order mail covers.

4. Excepting mail covers ordered upon subjects engaged, or suspected to be engaged, in any activity against the national security, or activity violative of any postal law, no mail cover order shall remain in force and effect for more than 30 days. At the expiration of such period, or prior thereto, the requesting authority may be granted additional 30-day periods under the same conditions and procedures applicable to the original request.

5. No mail cover shall remain in force longer than 120 days unless personally approved for further extension by the Chief Postal Inspector.

6. Excepting fugitive cases, no mail cover shall remain in force when the subject has been indicted for any cause. If the subject is under investigation for further criminal violations, a new mail cover order must be requested consistent with these regulations.

Records:

1. All requests for mail covers, with records of action ordered thereon, and all reports issued pursuant thereto, shall be deemed within the custody of the Chief Postal Inspector. However, the physical housing of this data shall be at the discretion of the Chief Postal Inspector.

2. The Postal Inspectors in Charge shall submit copies of all requests for mail covers to the Chief Postal Inspector, together with reports of the action ordered thereon.

3. If the Chief Postal Inspector determines a mail cover was improperly ordered by a Postal Inspector in Charge or his designee all data acquired while the cover was in force shall be destroyed, and the requesting authority notified of the discontinuance of the mail cover and the reasons therefor.

4. Any data concerning mail covers shall be made available to any mail cover subject in any legal proceeding through appropriate discovery procedures.

5. The retention period for files and records pertaining to mail covers shall be 8 years.

Reporting to Requesting Authority:

Once a mail cover has been duly ordered, authorization may be delegated to any officer in the Postal Service to transmit mail cover reports directly to the requesting authority. Where at all possible, the transmitting officer should be a Postal Inspector.

Review:

1. The Chief Postal Inspector, or his designee, shall review all actions taken by Postal Inspectors in Charge

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MAIL COVERS

(Continued from p. 2)

or their designees upon initial submission of a report on a request for mail cover.

2. The Chief Postal Inspector's determination in all matters concerning mail covers shall be final and conclusive and not subject to further administrative review.

• • • • •

Existing instructions will be revised accordingly. Postmasters shall not, under any conditions, place mail covers without prior approval from their Postal Inspectors in Charge.

Postmaster General.

All Postal Installations

Jet Airmail Service—AM-9

On or about July 4, 1965, Braniff Airways, Inc. will inaugurate jet airmail service from Waterloo, Iowa.

An official cachet will be furnished for application to philatelic covers transported only on Braniff's first jet flight departing from Waterloo on that day. The covers will be backstamped at the terminus of the flight.

The usual philatelic treatment, outlined in section 145.5, Postal Manual, will be provided.

Patrons desiring to receive this cachet should forward their covers in another cavelope to:

Postmaster
Waterloo, Iowa 50701

First-flight covers should reach Waterloo at least 5 days before the flight date.—*Bureau of Transportation and International Services, 6-17-65.*

All Postal Installations

Arrest of Postal Offender

The following postal offender has been apprehended:

Ronald Guy Picklesimer

Destroy the wanted circular concerning him.—*Bureau of the Chief Postal Inspector, 6-17-65.*

All Postal Installations

Field Printing and Duplicating

1. Purpose

These instructions will enable postal installations to manage their printing and duplicating activities more effectively. They are in line with the President's policy for reducing paperwork and for saving manpower and money. The new procedures are effective immediately.

2. Program for Improvement

Major efficiencies in the duplicating, copying, and publication areas can be achieved under these procedures. The program will assure that:

- Only necessary and justified publications are produced at the post office level.
- Only necessary equipment is rented or purchased.
- Printing and binding regulations of the Congressional Joint Committee on Printing are understood and followed.
- Duplicating and printing activities are consolidated wherever possible.
- Coordination of policy matters concerning duplicating and printing is achieved.
- Responsibilities in these areas are correctly placed and clearly understood.

3. Field Printing

Field offices with duplicating equipment must follow the provisions of Handbook M-13, Field Printing, Duplicating and Related Services. That handbook is being revised and will include all necessary information on the subject. It will be distributed directly to offices with duplicating equipment.

4. Procurement of Equipment

The Congressional Joint Committee on Printing requires that requests for printing and duplicating equipment be approved by qualified personnel. Therefore, all field requests (except those from the Inspection Service) for the purchase or rental of printing and duplicating equipment must be sent on Form 73 to the regional procurement and supply officer with a detailed justification so that he can obtain the necessary approval. There will be no exception to the foregoing procedure.

5. Managing Local Publications

This section establishes a program for managing local publications and keeping them within reasonable bounds. It applies only to formal types of publications—manuals, handbooks, pamphlets, booklets, and brochures. Office memorandums, schemes and schedules and changes thereto, and internal circular issuance systems are not affected.

Postmasters will submit proposed publications in outline form to the regional postal systems division for regional approval. Request for approval will include justification for the publication, the estimated number of printed pages, the quantity to be printed, and a list showing the number to be distributed to each receiving point.

If the postal systems division determines that the proposal meets the following criteria, it will secure approval of the Regional Director and return the outline to the post office for preparation of the final manuscript. The postal systems division will indicate whether the publication is to be reproduced at the post office or returned to the regional office for final printing.

Consider the following criteria thoroughly before requesting approval for a publication:

a. Is the proposed publication absolutely necessary? Local publications must be limited to those which are essential to the service.

b. Does the proposal repeat Headquarters, Postal Bulletin, Postal Manual or other instructions? Such repetition *must* be avoided.

c. If the publication is considered to be essential, how much will it cost? An estimated per page cost of $150 is considered a reasonable figure (General Services Administration uses $400 per page). This cost includes such factors as salaries, draft preparation, approval time, printing materials and equipment, and a factor for general overhead.

d. Does the proposal contain material which has nationwide possibility? If so, the postmaster should request the region to consider proposing a national publication.

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233.2 MAIL COVERS

.21 DEFINITION

A mail cover is the process by which a record is made of any data appearing on the outside cover of any class of mail matter, including checking the contents of any second-, third- or fourth-class mail matter as now sanctioned by law, to obtain information in the interest of (1) protecting the national security (2) locating a fugitive or (3) obtaining evidence of commission or attempted commission of a crime.

.22 AUTHORITY

Only the Chief Postal Inspector or his designee may order mail covers. Under no circumstances shall a postmaster or postal employee furnish information as defined in 233.21 to any person except as authorized by the Chief Postal Inspector or his designee.

[illegible] Housing Act of 1968 (Title XIII of the Housing and Urban Development Act of 1968, effective June 30, 1969 (82 Stat. 476), Sec. 28, 1969 (as amended, 42 U.S.C. 4001-4128), and Secretary's delegation of authority to National Insurance Administrator, 34 F.R. 2680, [illegible]

Issued: February 28, 1975.

J. Ronnie Greene,
Acting Federal Insurance Administrator.

[FR Doc.75-6723 Filed 3-11-75;8:45 am]

Title 39— Postal Service

CHAPTER I—UNITED STATES POSTAL SERVICE

PART 233—INSPECTION SERVICE AUTHORITY

Mail Covers

The Postal Service has decided to republish the regulations governing the use of the mail cover as an investigative technique to make these regulations more accessible to the public, and to discourage confusion concerning the nature and uses of this important law enforcement tool. In this republication the Postal Service has updated the provisions dealing with the delegation of mail cover authority to reflect the present organizational structure of the Postal Inspection Service. However, no substantive changes have been made in mail cover procedures or safeguards.

The use of mail covers has been governed by regulations contained in § 233.2 of the *Postal Service Manual*, supplemented by provisions formerly contained in Part 861 of the *Postal Manual* of the old Post Office Department which have been retained as operating instructions by the Postal Inspection Service. The consolidation of these provisions under one heading in the Code of Federal Regulations will improve their accessibility and facilitate their interpretation.

A mail cover is a relatively simple investigative or law enforcement technique. It involves recording the name and address of the sender, the place and date of postmarking, the class of mail, and any other data appearing on the outside cover of a piece of mail. Mail is not delayed in connection with a mail cover, and the contents of first-class mail are not examined. As sanctioned by law, the contents of second-, third-, and fourth-class mail matter may be examined in connection with a mail cover.

In their new format, the mail cover regulations of the Postal Service continue existing procedural and substantive safeguards designed to assure the confidentiality of the mail cover process and prevent the unjustified use of mail covers. Mail covers are available to law enforcement agencies only in order to obtain information in the interest of (1) protecting the national security, (2) locating a fugitive, or (3) obtaining evidence of commission or attempted commission of a crime. Mail covers are ordered pursuant to a written request from a law enforcement agency only if the requesting authority signatures and specifies the reasonable grounds that exist which demonstrate the mail cover is necessary for a legitimate purpose. No officers or employees of the Postal Service other than the Chief Postal Inspector, a Postal Inspector in Charge, and a limited number of their designees, are authorized to order mail covers. Only the Chief Postal Inspector, or his designees at Inspection Service Headquarters, may order a national security mail cover. Mail covers do not include matter mailed between the mail cover subject and his known attorney-at-law; and except in fugitive cases, no mail cover remains in force when the subject has been indicted for any crime. Any data concerning mail covers is made available to any mail cover subject in any legal proceeding through appropriate discovery procedures. These administrative safeguards afford significant protection to the privacy of the users of the mail, without compromising the effectiveness of the mail cover.

Accordingly, the Postal Service adopts the following amendments to the provisions concerning Postal Service management, organization, procedure, and practice with regard to mail covers, effective March 14, 1975:

§ 233.2 [Redesignated]

1. In 39 CFR Part 233, § 233.2 *Withdrawal of mail privileges* is renumbered as § 233.3, and a new § 233.2 is added to read as follows:

§ 233.2 Mail covers.

(a) *Policy.* The U.S. Postal Service maintains rigid controls and supervision with respect to the use of mail covers as investigative or law enforcement techniques.

(b) *Scope.* These regulations supersede the sole authority and procedure for initiating, processing, placing and using mail covers.

(c) *Definitions.* For purposes of these regulations, the following terms are hereby defined:

(1) "Mail cover" is the process by which a record is made of any data appearing on the outside cover of any class of mail matter, including checking the contents of any second-, third-, or fourth-class mail matter as now sanctioned by law, in order to obtain information in the interest of (i) protecting the national security, (ii) locating a fugitive, or (iii) obtaining evidence of commission or attempted commission of a crime.

(2) "Fugitive" is any person who has fled from the United States or any State, territory, the District of Columbia, or possession of the United States, to avoid prosecution for a crime, to avoid punishment for a crime or to avoid giving testimony in a criminal proceeding.

(3) "Crime", for purposes of these regulations, is any commission of an act or the attempted commission of an act that is punishable by law by imprisonment for a term exceeding 1 year.

(4) "Law enforcement agency" is any authority of the Federal Government or any authority of a State or local government one of whose functions is to investigate the commission or attempted commission of acts constituting a crime.

(d) *Authorization—Chief Postal Inspector.* (1) The Chief Postal Inspector is the principal officer of the Postal Service in the administration of all matters concerning mail covers. He may delegate any or all authority in this regard to not more than two designees at Inspection Service Headquarters. Except for national security mail covers, he may also delegate any or all authority to the Regional Chief Postal Inspectors. All such delegations of authority shall be issued through official directives.

(2) The Chief Postal Inspector, or his designee, may order mail covers under the following circumstances:

(i) When he has reason to believe the subject or subjects of the mail cover are engaged in any activity violative of any postal statute.

(ii) When written request is received from any law enforcement agency wherein the requesting authority stipulates and specifies the reasonable grounds that exist which demonstrate the mail cover is necessary to (A) protect the national security, (B) locate a fugitive, or (C) obtain information regarding the commission or attempted commission of a crime.

(iii) Where time is of the essence, the Chief Postal Inspector, or his designee, may act upon an oral request to be confirmed by the requesting authority in writing within 2 business days. However, no information shall be released until an appropriate written request is received.

(e) *Postal Inspectors in Charge.* (1) All Postal Inspectors in Charge and not more than three designees may act on delegations in writing. Any order mail covers within their districts under the following circumstances:

(i) Where he has reason to believe the subject or subjects are engaged in an activity violative of any postal statute.

(ii) Where written request is received from any law enforcement agency of the Federal, State, or local governments, wherein the requesting authority stipulates and specifies the reasonable grounds that exist which demonstrate the mail cover would aid in the apprehension of fugitives, or that it would assist in obtaining information concerning the commission or attempted commission of a crime.

(2) Except where mail covers are ordered by the Chief Postal Inspector, or his designee, requests for mail covers must be approved by the Postal Inspector in Charge, or his designee, in each district in which the mail cover is to operate.

(c)(2) Where there is of the opinion, the Postal Inspector in Charge, or his designee, may act upon an oral request to the addressee by the requesting authority in writing within 3 business days. However, no information shall be released until an appropriate written order is received.

(d) *Limitations.* (1) No person in the Postal Service, except those employed for that purpose in dead-mail offices, may detain or permit detaining of the mail of any matter mailed as first-class mail (domestic, seventh warrant), even though it may contain evidence or otherwise matter, or furnish evidence of the commission of a crime.

(2) No mail covers shall include matter mailed between the mail cover subject and his lawful attorney-at-law.

(3) No officer or employee of the Postal Service other than the Chief Postal Inspector, or Postal Inspectors in Charge, and their assignees, are authorized to order mail covers. Under no circumstances shall a postmaster or postal employee furnish information as defined in § 233.2(e) to any person except as authorized by the Chief Postal Inspector, a Postal Inspector in Charge, or those designees.

(4) Executing mail covers ordered upon subjects engaged, or suspected to be engaged, in any activity against the national security, or activity violative of any postal law, no mail cover order shall remain in force and effect for more than 30 days. At the expiration of such period, or prior thereto, the requesting authority may be granted additional 30-day periods under the same conditions and procedures applicable to the original request.

(5) No mail cover shall remain in force longer than 120 days unless personally approved for further extension by the Chief Postal Inspector.

(6) Executing fugitive cases, no mail cover shall remain in force when the subject has been indicted for any crime. If the subject is under investigation for further criminal violations, a new mail cover order may be requested consistent with these regulations.

(e) *Records.* (1) All requests for mail covers, with records of action ordered thereon, and all reports issued pursuant thereto, shall be deemed within the custody of the Chief Postal Inspector. However, the physical housing of this data shall be at the discretion of the Chief Postal Inspector.

(2) The Postal Inspectors in Charge shall promptly submit copies of all requests for mail covers and the determinations made thereon to the Chief Postal Inspector, or to his designee for review.

(3) If the Chief Postal Inspector, or his designee, determines a mail cover was improperly ordered by a Postal Inspector in Charge or his designee all data acquired while the cover was in force shall be destroyed, and the requesting authority notified of the circumstances of the mail cover and the reasons therefor.

(f) *Any data concerning mail covers* shall be made available to any mail cover subject in any legal proceeding through appropriate discovery procedures.

(2) The retention period for files and records pertaining to mail covers shall be 8 years.

(h) *Reporting to Requesting Authority.* Once a mail cover has been duly ordered, authorization may be delegated to any officer in the Postal Service to transmit mail cover reports directly to the requesting authority. Where at all possible, the transmitting officer should be a Postal Inspector.

(i) *Records.* (1) The Chief Postal Inspector, or his designee, shall review all actions taken by Postal Inspectors in Charge or their designees upon initial submission of a request or a request for mail cover.

(2) The Chief Postal Inspector's determination in all matters concerning mail covers shall be final and conclusive and not subject to further administrative review.

2. In the table of sections of 39 CFR Part 233 the following entries are revised to read as follows:

Sec.
233.1 Definitions and records.
233.2 Mail covers.
233.3 Withdrawal of mail privileges.

(39 U.S.C. 401, 404, 4101)

Rosser F. Cecil,
Deputy General Counsel.

[F.R. Doc. 65-6269 Filed 6-15-65; 8:45 am]

Title 41—Public Contracts and Property Management

CHAPTER 1—FEDERAL PROCUREMENT REGULATIONS

[FPR Amdt. 128]

PART 1-7—CONTRACT CLAUSES

Subcontracts

This amendment of the Federal Procurement Regulations prescribes a new subcontracts clause for use in fixed-price supply and construction contracts. The clause requires the contractor to obtain the contracting officer's written consent prior to entering into certain types and dollar values of subcontracts. The clause becomes operative only with respect to negotiated modifications under fixed-price contracts. Adoption of the clause reflects a significant part of Recommendation A-37 of the Commission on Government Procurement. This amendment also adds a requirement for the submission of cost accounting standards information in connection with subcontracts under cost-reimbursement type supply contracts, and incorporates a new reference to the clause requiring the payment of interest on equitable[d] claims.

The table of contents for Part 1-7 is changed to add new entries as follows:

Sec.
1-7.103-23 Payment of interest on contractors' claims.
1-7.103-37 Subcontracts.
1-7.103-38 Subcontracts.

Subpart 1-7.1—Fixed-Price Supply Contracts

1. Section 1-7.102 required clauses is amended by the addition of § 1-7.103-23 as follows:

§ 1-7.103-23 Payment of interest on contractors' claims.

Insert the clause set forth in § 1-7.103 under the conditions prescribed therein.

2. Section 1-7.103 Clauses to be used when applicable is amended by the addition of § 1-7.103-37 as follows:

§ 1-7.103-37 Subcontracts.

The following clause may be inserted in fixed-price supply contracts whenever it is likely that subsequent to award major modifications will be initiated pursuant to the Changes clause, or other contract provisions, and that such modifications will result in the placement of additional subcontracts. The pricing arrangements of such subcontracts can be impact upon the fixed price of the modifications; therefore, it is essential that they be made available to the contracting officer for review by the contracting officer (see §§ 1-3.807-1(d)(5) and 1-3.808).

(The provisions of this clause do not apply to fixed-price and fixed price [illegible] contracts. The clause does apply to most subcontracts or modifications of existing subcontracts which are expected to have a value of [illegible] contract changes pursuant to the Changes clause or other provisions of this contract.)

(a) As used in this clause, the term "subcontract" has the following meaning.

(b) The Contractor shall notify the Contracting Officer reasonably in advance of entering into any subcontract if the Contractor's procurement system has not been approved by the Contracting Officer and if this subcontract:

(i) Is to be a cost-reimbursement, time and materials, or labor-hour contract which is estimated will involve an amount in excess of [illegible] including any fee;

(ii) Is proposed to exceed one hundred thousand dollars ($100,000); or

(iii) Is one of a number of subcontracts, under this contract, with a single subcontractor for the same or related supplies or services which, in the aggregate, are expected to exceed one hundred thousand dollars ($100,000).

(c) The advance notification required by paragraph (b) above shall include:

(i) A description of the supplies or services to be called for by the subcontract;

(ii) Identification of the proposed subcontractor and an explanation of why and how the proposed subcontractor was selected, including the competition obtained;

(iii) The proposed subcontract price, together with the Contractor's cost or price analysis thereof;

(iv) The subcontractor's current, complete, and accurate cost or pricing data and Certificate of Current Cost or Pricing Data, when such data and certification are required by other provisions of this contract, or the refusal from the subcontractor;

(v) Identification of the type of subcontract to be used;

(vi) A negotiation of negotiation objectives for the principal elements of the subcontract price negotiations. A copy of this memorandum shall be attached to the Contractor's file for use of Government reviewing authorities. The memorandum shall be in sufficient detail to reflect the results of significant considerations in establishing the negotiation of initial or revised prices. The memorandum should include an explanation of why cost or pricing data was, or was not